HAMPSHIRE COUNTY COUNCIL

Decision Report

Decision Maker:	Audit Committee
Date:	29 September 2021
Title:	Treasury Management Mid-Year Monitoring Report 2021/22
Report From:	Director of Corporate Operations

Contact name: Gemma Farley

Tel: 03707 794704 **Email:** Gemma.farley@hants.gov.uk

Purpose of the report

1. The County Council has adopted the key recommendations of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code), last updated in 2017. The CIPFA Code requires the County Council to approve a treasury management strategy before the start of the year and a semi-annual and annual treasury outturn report. The purpose of this report is therefore to meet this obligation by providing an update on the performance of the treasury management function at the mid-year point.

Recommendation

2. The Audit Committee are asked to note the following recommendations that are being reported to Cabinet:

   - That the mid-year review of treasury management activities be noted.

   - That the clarification to the 2021/22 Treasury Management Strategy as set out in paragraph 36, for investments in un-rated corporations where the County Council owns a controlling interest in the corporation, is approved in line with previous years' strategies.

Executive Summary

3. The report fulfils the County Council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code and provides an update on the performance of the treasury management function during 2021/22.

4. The County Council's treasury management strategy was most recently updated and approved at a meeting of Full County Council in February 2021. The County Council has borrowed and invested sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the County Council's treasury management strategy.

5. Treasury management in the context of this report 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."

6. This report sets out the performance of the treasury management function from the beginning of April to the end of August 2021, to include the effects of the decisions taken and the transactions executed.

7. All treasury activity has complied with the County Council's Treasury Management Strategy and Investment Strategy for 2021/22, and all relevant statute, guidance and accounting standards. In addition, support in undertaking treasury management activities has been provided by the County Council's treasury advisers, Arlingclose.

8. The 2017 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The County Council's Capital and Investment Strategy, complying with CIPFA's requirement, was approved by full County Council on 25 February 2021.

External Context

9. The following sections outline the key economic themes against which investment and borrowing decisions have been made so far in 2021/22.

Economic commentary

10. The coronavirus pandemic continued to dominate the news during the period, with economic resurgence following the initial rapid vaccination programme.

11. The Bank of England (BoE) has held Bank Rate at 0.1% since March 2020 and has maintained its Quantitative Easing programme at £895bn since November 2020. The BoE expects the economy to experience a temporary

period of strong Gross Domestic Product (GDP) growth and above-target Consumer Price Index (CPI) inflation, after which growth and inflation is expected to fall back. There were, however, two-sided risks around this central path, and it is possible that near-term upward pressure on prices could prove somewhat larger than expected. The BoE's Monetary Policy Committee (MPC) does not intend to tighten monetary policy at least until there is clear evidence that significant progress is being made in eliminating the economy's spare capacity and achieving the 2% inflation target sustainably.

Financial markets

12. Ongoing monetary and fiscal stimulus together with improving economic growth prospects and successful vaccine rollout programmes continued to boost equity markets over the period. In the UK, the FTSE 250 index was back above pre-pandemic levels and the more internationally focused FTSE 100 had recouped around 75% of 2020's losses.

13. Inflation worries continued during the period but declines in bond yields between April and June suggest bond markets may be expecting any general price increases to be less severe, or more transitory, than was previously thought. UK government bonds remained positive but sold off over the period.

Credit review

14. Credit default swap spreads were relatively flat over the period and remained only slightly above their pre-pandemic levels. Credit default swaps are used as an indicator of credit risk, where higher premiums indicate higher perceived risks.

15. There were only a small number of credit rating actions over the period including Fitch revising the United Kingdom's outlook to stable from negative, and S&P upwardly revising the outlooks for a number of UK and European banks from negative to stable, or in the case of Barclays and Nationwide from stable to positive.

16. The successful vaccine rollout programme is credit positive for the financial services sector in general, but there remains uncertainty around the extent of the losses banks and building societies will suffer due to the economic slowdown which has resulted due to the pandemic and the effects of lockdowns and restrictions. This uncertainty means the County Council's treasury management advisors, Arlingclose, continue to recommend maximum durations of 35 days for unsecured investments with banks and building societies on their list of recommended counterparties.

Local Context

17. On 31 March 2021, the County Council's underlying need to borrow for capital purposes was £776.46m as measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment and amounted to £877.8m. These factors are summarised in Table 1.

Table 1: Balance sheet summary	**31/03/21 Balance £m**
CFR	776.46
Less: Other debt liabilities*	(141.47)
Borrowing CFR	**634.99**
External Borrowing	(300.77)
Internal Borrowing	**334.22**
Less: Usable Reserves	(754.85)
Less: Working Capital	(122.91)
Net Investments	**(543.54)**

* PFI liabilities that form part of the County Council's total debt

18. The County Council's current strategy is to maintain borrowing and investments below their underlying levels, referred to as internal borrowing, to reduce risk and keep interest costs low. The treasury management position as at 31 August 2021 and the movement since 31 March 2021 are shown in Table 2.

Table 2: Treasury management summary	**31/03/21 Balance £m**	**Movement £m**	**31/08/21 Balance £m**	**31/08/21 Rate %**
Long-term borrowing	(249.3)	2.1	(247.2)	4.65
Short-term borrowing	(8.5)	(1.5)	(10.0)	5.75
Total borrowing	**(257.8)**	**0.6**	**(257.2)**	**4.70**
Long-term investments	259.9	(24.8)	235.1	1.50
Short-term investments	194.7	229.2	423.9	0.15
Cash and cash equivalents	112.5	(101.6)	10.9	0.00
Total investments	**567.1**	**102.9**	**669.9**	**1.65**
Net investments	**309.3**	**103.4**	**412.7**	

Note: the figures in Table 2 at 31 March 2021 are from the balance sheet in the County Council's statement of accounts, but adjusted to exclude operational cash, accrued interest and other accounting adjustments. Borrowing figures exclude short term balances held on behalf of others. For these reasons Net investments in Table 2 differs from Table 1.

19. The increase in net investments of £103.4m shown in Table 2 reflects a large increase in total investments as well as a reduction in total borrowing. The reduction in total borrowing of £0.6m reflects the repayment of debt in line with scheduled timescales. The increase of £103.4m of investments reflects the higher balances typically seen at this time of year, due to the difference in timing between income and expenditure; investment balances have also been impacted by the fact that it is near to the half-way point of the three-year period that the County Council pre-paid Pension Fund contributions for, and so it is expected that underlying core balances will continue to rise until the end of this three-year period.

Borrowing Update

20. Local authorities can borrow from the Public Works Loan Board (PWLB) provided they have not purchased an investment asset primarily for yield since 26 November 2020 and can confirm they are not planning to do so in the current or next two financial years, with confirmation of the purpose of capital expenditure from the Section 151 / Section 95 Officer. Authorities that are purchasing or intending to purchase investment assets primarily for yield will not be able to access the PWLB except to refinance existing loans or externalise internal borrowing.

21. Acceptable use of PWLB borrowing includes service delivery, housing, regeneration, preventative action, refinancing and treasury management.

22. The County Council is not planning to purchase any investment assets primarily for yield within the next three years and so is able to fully access the PWLB if required, however there are no plans to take out any new long-term external borrowing.

Borrowing Activity

23. At 31 August 2021 the County Council held £257.2m of loans (a decrease of £0.6m since 31 March 2021) as part of its strategy for funding previous years' capital programmes. The mid-year treasury management borrowing position and movement since 31 March 2021 are shown in Table 3.

Table 3: Borrowing position	31/03/21 Balance £m	Net movement £m	31/08/21 Balance £m	31/08/21 Weighted average rate %	31/08/21 Weighted average maturity (years)
Public Works Loan Board	(216.5)	0.5	(216.0)	4.74	10.32
Banks (LOBO)	(20.0)	-	(20.0)	4.76	11.96
Other (fixed term)	(21.3)	0.1	(21.2)	4.16	18.38
Total borrowing	**(257.8)**	**0.6**	**(257.2)**	**4.70**	**11.11**

Note: the figures in Table 3 at 31 March 2021 are from the balance sheet in the County Council's statement of accounts but adjusted to exclude short term balances held on behalf of others, and accrued interest.

24. The County Council's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the County Council's long-term plans change is a secondary objective.

25. Short-term interest rates have remained much lower than long-term rates and the County Council has therefore considered it to be more cost effective in the near term to use internal resources than to use additional borrowing. In line with this strategy, £0.5m of PWLB loans and £0.1m of Salix loans were allowed to mature without refinancing. Salix loans represent Government funding given to improve energy efficiency, reduce carbon emissions and lower energy bills.

26. This borrowing strategy has been monitored with the assistance of Arlingclose and has enabled the County Council to reduce borrowing costs (despite foregone investment income) and reduce overall treasury risk.

27. The County Council continues to hold £20.0m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the County Council has the option to either accept the new rate or to repay the loan at no additional cost. None of the LOBO loan options were exercised by the lender during the period.

Treasury Investment Activity

28. The County Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the five-month period from 1 April to 31 August 2021, the County Council's investment balances ranged between £562m and £769m due to timing

differences between income and expenditure. The investment position as at 31 August 2021 and the change since 31 March 2021 are shown in Table 4.

Table 4: Treasury investment position	**31/03/21 Balance £m**	**Net movement £m**	**31/08/21 Balance £m**	**31/08/21 Income return %**	**31/08/21 Weighted average maturity (years)**
Short term investments					
Banks and building societies:					
- Unsecured	69.5	45.1	114.6	0.06	0.06
- Secured	10.7	111.2	121.9	0.13	0.63
Government:					
- Local authorities	139.0	(2.0)	137.0	0.49	0.50
- UK treasury bills	0.0	15.0	15.0	0.05	0.15
- UK Gilts	0.0	20.0	20.0	0.03	0.02
Money market funds	78.0	(74.2)	3.8	0.02	0.00
Cash plus funds	10.0	-	10.0	0.79	0.01
	307.2	**115.1**	**422.3**	**0.23**	**0.38**
Long term investments					
Banks and building societies					
- Secured	20.0	12.5	32.5	0.20	1.16
Government:					
- Local authorities	35.0	(25.0)	10.0	0.71	1.18
	55.0	**(12.5)**	**42.5**	**0.47**	**1.34**
Long term investments – higher yielding strategy					
Government:					
- Local authorities	21.7	0.2	21.9	4.38	11.99
Pooled funds:					
- Pooled property*	75.0	-	75.0	4.18	N/A
- Pooled equity*	50.0	-	50.0	6.08	N/A
- Pooled multi-asset*	48.0	-	48.0	4.66	N/A
	194.7	**0.2**	**194.9**	**4.81**	**11.99**
Total investments	**556.9**	**102.8**	**659.7**	**1.59**	**0.72**
Thames Basin Heaths pooled fund investments	10.2	0.0	10.2		
Total	**567.1**	**102.8**	**669.9**		

* The rates provided for pooled fund investments are reflective of annualised income returns over the year to 30 June 2021 based on the market value of investments 12 months earlier.

Note: the figures in Table 4 at 31 March 2020 are from the balance sheet in the County Council's statement of accounts, but adjusted to exclude operational cash, accrued interest and other accounting adjustments.

29. The County Council made a payment of £226.7m on 1 April 2020 to prepay its employer's LGPS pension contributions for a period of three years. By making this payment in advance the County Council was able to generate an estimated saving of £9m over 3 years on its pension contributions. It is expected that cash balances will steadily increase over this three year period in addition to the normal cash movements due to timing differences between income and expenditure.

30. Investment balances have subsequently increased and were £102.8m higher at 31 August 2021 in comparison to the position at 31 March 2021. This is in part explained by the County Council not having to make monthly employer's pension contributions in 2021/22 (having already paid in advance) and the balance of grants received but not yet applied. The impact of the coronavirus pandemic has created significant uncertainty, resulting in the need for significant assumptions within financial forecasts and a difference in timing between income and expenditure, both in terms of the direct response to the pandemic and in carrying out regular service delivery plans.

31. The CIPFA Code and government guidance both require the County Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The County Council's objective when investing money is therefore to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults against the risk of receiving unsuitably low investment income. The County Council's Treasury Management Strategy Statement (TMSS) sets out how it will manage and mitigate these risks.

32. The security of investments has been maintained by following the County Council's counterparty policy and investment limits within the TMSS, taking advice from Arlingclose on changes in counterparty credit worthiness, and making use of secured investment products that provide collateral. The County Council invests in liquid investments to ensure money is available when required to meet its financial obligations, spreading these investments across a number of counterparties to mitigate operational risk.

33. In delivering investment returns, the County Council has operated against a backdrop in which the UK Bank Rate was cut to 0.10% in March 2020 in response to the coronavirus pandemic. UK Bank Rate has remained at this rate, having an impact on rates across the market. Returns had been at or around 0% for liquid investment options such as Money Market Funds (MMFs), bank call accounts and the UK Government's Debt Management Account Deposit Facility (DMADF) and have not been significantly higher for

other short-term options like fixed duration loans to other local authorities and bank notice accounts. Investment income has therefore largely come from investments arranged at fixed rates of interest prior to the pandemic and through the County Council's investments in pooled funds.

34. The County Council benchmarks the performance of its internally managed investments against that of other Arlingclose clients on a quarterly basis. Internally managed investments include all investments except externally managed pooled funds but do include MMFs. The performance of these investments against relevant measures of security, liquidity and yield are shown in Table 5, providing data for the quarter ended 31 June 2021 and at 31 March 2021 for comparison.

Table 5: Investment benchmarking (excluding pooled funds)	**Credit rating**	**Bail-in exposure %**	**Weighted average maturity (days)**	**Rate of return %**
31.03.2021	AA-	40	393	0.50
30.06.2021	AA-	34	345	0.39
Similar LAs	AA-	45	1,101	0.30
All LAs	A+	67	12	0.11

35. Table 5 shows the average credit rating of the portfolio has remained consistent over the three-month period, whilst bail-in exposure has reduced, as the County Council held a greater investment balance in secured bank bonds, which are not subject to bail-in risk as they provide collateral. The weighted average maturity of investments was lower due to the increase in total investment balance being held in short-term investment options, ensuring that funds will be available as required. In addition, there were timing differences between receiving and spending of Covid grants. The average rate of return (0.39%) was lower than at 31 March 2021, but with the benefit of higher rates for fixed investments made prior to the pandemic helping to offset returns at or close to 0% for many investments across the market. The County Council compared favourably with the other local authorities included in the benchmarking exercise across all metrics.

36. The County Council's Treasury Management Strategy (TMSS) for 2020/21 and prior, contained a clause that the County Council could invest in an un-rated corporation where it owns a controlling interest in the corporation, in which case a limit of £35m for an investment of up to 20 years will apply. This was unintentionally not included in the 2021/22 TMSS, and it is therefore recommended that this clause is reinstated for the continuity of this policy.

Externally managed pooled funds

37. In 2019 the County Council agreed to increase the amount of its cash balances earmarked for investments targeting higher yields of around 4% to £235m. This allocation was recently increased to £250m as part of the Capital and Investment Strategy for 2021/22 and the approach to investing this allocation was most recently set out in the Treasury Management Strategy Statement for 2021/22.

38. Approximately £205m of this allocation has now been invested, with the remaining balance earmarked. The total includes £10.4m invested on behalf of the Thames Basin Heaths Joint Strategic Partnership Board (TBH JSPB), where the County Council acts as the administrative body. Any investments made from cash held on behalf of the TBH JSPB are made with the agreement that the TBH JSPB has received its own financial advice and assumes all risks associated with these investments.

39. The CIPFA Code requires the County Council to invest its funds prudently and to have regard to the security and liquidity of its investments before seeking the highest yield. As a result, the County Council's investments targeting higher yields have been made from its most stable balances and with the intention that they will be held for at least the medium term. This means that the initial costs of any investment and any periods of falling capital values can be overcome and mitigates the risk of having to sell an asset for liquidity purposes, helping to ensure the long-term security of the County Council's investments.

40. The County Council's investments in pooled funds fell considerably in value when the coronavirus pandemic hit world markets but have since recovered well reflecting improved market sentiment. These investments are now worth more in aggregate than the initial sums invested, as shown in Table 6, demonstrating the importance of taking a longer term approach and being able to ride out periods of market volatility, ensuring the County Council is not a forced seller at the bottom of the market. Table 6 also shows the County Council's investments in fixed deposits which include long term loans to other local authorities and as part of the Manydown programme.

Table 6: High yielding investments – market value performance	**Amount invested***	**Market value at 30/06/21**	**Gain / (fall) in capital value**	
			Since purchase	**One year**
	£m	**£m**	**£m**	**£m**
Pooled property funds	75.0	77.2	2.2	4.4
Pooled equity funds	50.0	50.8	0.8	8.6

Pooled multi-asset funds	48.0	48.7	0.7	3.0
Total pooled funds	**173.0**	**176.7**	**3.7**	**16.1**
Fixed deposits	21.9	21.9	0.0	0.0
Total higher yielding	**194.9**	**198.5**	**3.7**	**16.1**

* excludes £10.4m invested on behalf of Thames Basin Heaths JSPB

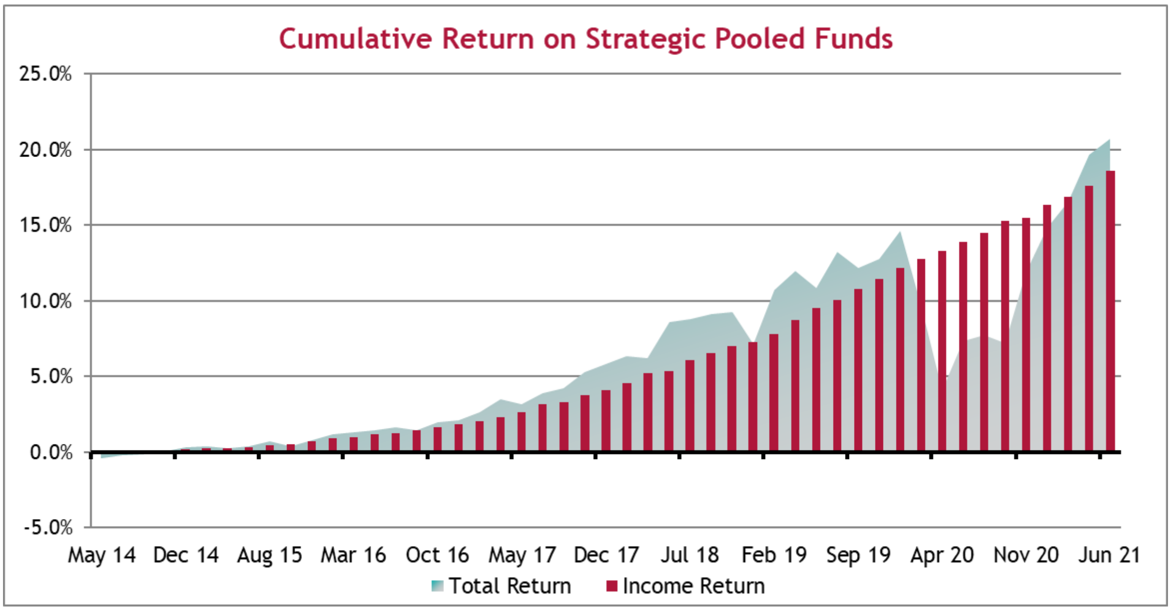
41. The County Council's investments in pooled funds target long-term price stability and regular revenue income and bring significant benefits to the revenue budget. As shown in Table 7 the annualised income returns have averaged 4.40% pa (per annum) since purchase against the higher yielding strategy target of 4% pa, contributing to a total return of 20.73%.

Table 7: High yielding investments – income and total returns since purchase	**Annualised income return**	**Total return**
	%	**%**
Pooled property funds	4.11	23.96
Pooled equity funds	4.99	22.35
Pooled multi-asset funds	4.30	14.03
Total pooled funds	**4.40**	**20.73**

Note: excludes the performance related to £10.4m invested on behalf of Thames Basin Heaths JSPB.

42. The County Council's pooled fund investments continue to deliver income returns far in excess of what could be generated from cash investments and in line with the County Council's agreed objective of targeting income of 4% pa from its higher yielding strategy.

43. The cumulative total return from the County Council's investments in pooled equity, property, and multi-asset funds since purchase is shown in the following graph. This highlights that the Count Council has benefited from strong and steady income returns over time and the way that capital values have recovered since March 2020.



Note: the graph above excludes the performance related to £10.4m invested on behalf of Thames Basin Heaths JSPB.

44. The County Council is aware of the risks involved with investing in pooled funds that hold underlying investments in bonds, equities, property and other financial instruments. As a result, when the County Council began to specifically target higher returns from a proportion of its investments, it also established an Investment Risk Reserve to mitigate the risk of an irrecoverable fall in the value of these investments. The balance held in this reserve is currently £6.25m which equates to 2.5% of the total earmark of £250m.

45. In addition to the risk of realising a capital loss, the IFRS 9 accounting standard that was introduced in 2018/19 means that annual movements in the capital values of investments need to be reflected in the revenue account on an annual basis, although a five year statutory override was put in place for local authorities that exempts them from complying with this requirement.

46. Pooled fund investments have no defined maturity date but are available for withdrawal after a notice period and their performance and continued suitability in meeting the County Council’s investment objectives is monitored regularly and discussed with Arlingclose.

Non-Treasury Investments

47. The definition of investments in CIPFA’s revised Treasury Management Code now covers all the financial assets of the County Council as well as other non-financial assets which the Council holds primarily for financial return. This is replicated in Ministry of Housing, Communities and Local Government’s Investment Guidance, in which the definition of investments is

further broadened to also include all such assets held partially for financial return.

48. This could include loans made to Hampshire based businesses or the direct purchase of land or property and such loans and investments will be subject to the County Council’s normal approval process for revenue and capital expenditure and need not comply with the treasury management strategy.

49. The County Council’s existing non-treasury investments are listed in Table 8.

Table 8: Non-Treasury Investments	**31/08/21 Asset value £m**	**31/08/21 Rate %**
Loans to Hampshire based business	9.5	4.00
Joint venture recruitment agency	0.2	5.00
Total	9.7	4.02

Compliance Report

50. The County Council confirms compliance of all treasury management activities undertaken during the period covered by this report with the CIPFA Code of Practice and the County Council’s approved Treasury Management Strategy.

51. Compliance with the authorised limit and operational boundary for external debt, is demonstrated in Table 9.

Table 9: Debt Limits	**2021/22 Maximum £m**	**31/08/21 Actual £m**	**2021/22 Operational Boundary £m**	**2021/22 Authorised Limit £m**	**Complied?**
Borrowing	258	257	740	810	✓
PFI and Leases	141	141	140	170	✓
Total debt	**399**	**398**	**880**	**980**	✓

52. Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure. Although PFI and Leases debt has been above its Operational Boundary during 2021/22 to date by a minimal amount, total debt has been well below the total Operational Boundary for the entire period. It is expected that the PFI and Leases debt will fall below its Operational Boundary by 31 March 2022 following the next payment, and there are no plans for any increase in PFI liabilities.

Treasury Management Indicators

53. The County Council measures and manages its exposures to treasury management risks using the following indicators.

Interest rate exposures

54. The following indicator shows the sensitivity of the County Council's current investments and borrowing to a change in interest rates.

Table 10: Interest rate risk indicator	31/08/21 Actual	Impact of +/-1% interest rate change
Sums subject to variable interest rates		
Investment	£462m	+/- £4.6m
Borrowing	£10m	+/- £0.1m

55. Fixed rate investments and borrowings are those where the rate of interest is fixed for a year. Instruments that mature within the year are classed as variable rate.

Maturity structure of borrowing

56. This indicator is set to control the County Council's exposure to refinancing risk. The upper and lower limits show the maximum and minimum maturity exposure to fixed rate borrowing as agreed in the Treasury Management Strategy Statement.

Table 11: Refinancing rate risk indicator	31/08/21 Actual	Upper Limit	Lower Limit	Complied
Under 12 months	4%	50%	0%	✓
12 months and within 24 months	2%	50%	0%	✓
24 months and within 5 years	11%	50%	0%	✓
5 years and within 10 years	21%	75%	0%	✓
10 years and within 20 years	52%	75%	0%	✓
20 years and within 30 years	9%	75%	0%	✓
30 years and above	0%	100%	0%	✓

57. The County Council holds £20m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate as set dates, following which the County Council has the option to either accept the new rate or to repay the loan at no additional cost. If not repaid before maturity, these loans have an average maturity date of 12 years (minimum 6 years; maximum 24 years).

Principal sums invested for periods longer than a year

58. The purpose of this indicator is to control the County Council’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:

Table 12: Price risk indicator	2021/22	2022/23	2023/24
Actual principal invested beyond year end	£235m	£205m	£205m
Limit on principal invested beyond year end	£350m	£330m	£300m
Complied?	✓	✓	✓

59. The table includes investments in strategic pooled funds of £183m as although these can usually be redeemed at short notice, the County Council and Thames Basin Heaths intend to hold these investments for at least the medium-term.

CIPFA consultations

60. In February 2021 CIPFA launched two consultations on changes to its Prudential Code and Treasury Management Code of Practice. These follow the Public Accounts Committee’s recommendation that the prudential framework should be further tightened following continued borrowing by some authorities for investment purposes. The revised codes are yet to be released, however CIPFA have released feedback documents following the February 2021 consultations, and the expected changes for the Codes are listed in the following paragraphs.

Prudential Code

61. The new Prudential Code is expected to add clarification and definitions for commercial activity and investment, and state that an authority must not borrow to invest for the primary purpose of commercial return.

62. The Prudential Code is expected to include the acceptable reasons to borrow money:

    i. financing capital expenditure primarily related to delivering a local authority’s functions,

    ii. temporary management of cash flow within the context of a balanced budget,

iii. securing affordability by removing exposure to future interest rate rises and

iv. refinancing current borrowing, including replacing internal borrowing.

63. In addition, proportionality will be included as an objective, and so will include new indicators for net income from commercial and service investments to net revenue stream. There will also be a specific objective around commercial investment with the intention of embedding good practice across authorities.

Treasury Management Code

64. The new Treasury Management Code is expected to seek to strengthen decision making by including the liability benchmark as a mandatory treasury indicator. A treasury management knowledge and skills framework will also be implemented to improve knowledge in a specialist area. In addition CIPFA is expected to incorporating Environmental, Social and Governance (ESG) issues as a consideration within TMP (Treasury Management Practice) 1 Risk Management.

Arlingclose's outlook for the remainder of 2021/22

65. The medium-term global economic recovery has continued with the reopening of economies and most look set to grow at a decent pace. Recovery in world demand has been more highly concentrated in goods than in services. The UK has continued to benefit from its initial rapid vaccine rollout, which appears to have weakened the link between infections and hospitalisations.

66. The re-opening the UK economy will result in improved GDP in Quarters 2 3 although the 'pingdemic' in June and July will have restrained activity a little and exacerbated labour shortages. The more upbeat assessment is that GDP will return to its pre-Covid peak by the end of December 2021 but will be predicated on the extent and speed with which households and businesses normalise their spending and activity during the remainder of the year.

67. Inflation rose to 2.5% in June. Alongside the increase in commodity and energy prices, supply and transportation bottlenecks and the boost in prices from the lifting of restrictions, the MPC has acknowledged the potential of CPI rising to around 4% in Quarter 4 2021. However, the transitory factors affecting inflation including the low base effect of 2020 are expected to unwind over time; expectations for medium-term inflation are not elevated.

68. There is uncertainty over the size and pace of change in the labour market as companies to adjust their staffing levels and new hires to post-Covid demand and working arrangements. The number of furloughed jobs has declined and the scheme ends in September 2021.

69. Government bond yields declined after rising earlier in the year as the prospect of imminent higher policy rates receded - the Delta variant increased concerns that the pandemic will dampen confidence and weigh on growth for longer than previously expected. Some upward pressure on gilt yields could remain in the short term due to the variability of data.

70. Policymakers have begun signalling their intention of higher policy rates, albeit not just yet. At its August 2021 meeting, the MPC indicated that some modest tightening of monetary policy over the 3-year forecast period was likely to be necessary to mitigate inflation risks. At its June 2021 meeting, the majority of members of the US Federal Open Market Committee (FOMC) expected to increase the US federal funds rate (current range 0%-0.25%) twice by the end of 2023.

71. Arlingclose expects Bank Rate to remain at the current 0.10% level. Arlingclose believe the risk of movement in the immediate term remains low, although the risks over the MPC’s 3-year horizon have increased and are leaning to the upside.

72. Gilt yields have fallen recently, but volatility is likely given the uncertainties over the economic outlook and central bank asset purchase programmes.

73. Longer term yields may face upward pressure towards the end of our forecast period as the economy moves back to a sustained footing and policy expectations start to strengthen.

74. Downside risks remain – the risk of further virus mutations including the Delta variant could destabilise the recovery. Downside risks also arise from potential future vaccine shortages as the demand for vaccines increases.

	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24
Official Bank Rate													
Upside risk	0.15	0.15	0.15	0.15	0.30	0.30	0.30	0.40	0.40	0.40	0.40	0.40	0.40
Arlingclose Central Case	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
Downside risk	-0.10	-0.10	-0.10	-0.10	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15	-0.15

Consultation, Equalities and Climate Change Impact Assessment

75. This report deals with the treasury management mid-year position for 2021/22, which is within year reporting matter and therefore no consultation or Equality Impact Assessments are required.

76. Hampshire County Council utilises two decision-making tools to assess the carbon emissions and resilience of its projects and decisions. These tools provide a clear, robust, and transparent way of assessing how projects, policies and initiatives contribute towards the County Council's climate change targets of being carbon neutral and resilient to the impacts of a 2℃ temperature rise by 2050. This process ensures that climate change considerations are built into everything the Authority does.

77. This report deals with the outturn position for the treasury management aspect of the County Council's business. In line with the CIPFA code, the County Council's treasury management investment balances are invested prioritising security, liquidity and then yield. The County Council's investments in pooled funds, which include investments in equities and bonds issued by a number of companies with exposures to a variety of issues, including those associated with Climate Change. All of the County Council's pooled funds are managed by investment managers who are signatories to the PRI (Principles for Responsible Investment), managing investments in line with their own individual responsible investment policies. The County Council's Treasury Management Advisers, Arlingclose, have advised the County Council on the suitability and selection of its pooled funds, including the investment managers' management of Environmental, Social and Governance (ESG) issues including the impact of Climate Change.

78. There are no further climate change impacts as part of this report which are concerned with financial reporting.

REQUIRED CORPORATE AND LEGAL INFORMATION:

Links to the Strategic Plan

This proposal does not link to the Strategic Plan but, nevertheless, requires a decision because it relates to the effective management of the County Council's cash balances.

Other Significant Links

Links to previous Member decisions:	
Title	Date
Direct links to specific legislation or Government Directives	
Title	Date

Section 100 D - Local Government Act 1972 - background documents	
The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)	
Document	Location
None	

EQUALITIES IMPACT ASSESSMENT:

1. Equality Duty

   The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

   - Eliminate discrimination, harassment and victimisation and any other conduct prohibited by or under the Act with regard to the protected characteristics as set out in section 4 of the Act (age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation);
   - Advance equality of opportunity between persons who share a relevant protected characteristic within section 149(7) of the Act (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, sex and sexual orientation) and those who do not share it;
   - Foster good relations between persons who share a relevant protected characteristic within section 149(7) of the Act (see above) and persons who do not share it.

   Due regard in this context involves having due regard in particular to:

   - The need to remove or minimise disadvantages suffered by persons sharing a relevant protected characteristic that are connected to that characteristic;
   - Take steps to meet the needs of persons sharing a relevant protected characteristic that are different from the needs of persons who do not share it;
   - Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity in which participation by such persons is disproportionally low.

2. Equalities Impact Assessment:

Equalities objectives are not expected to be adversely impacted by the proposals in this report.