Public

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DERBYSHIRE COUNTY COUNCIL

CABINET

10 December 2020

Report of the Director of Finance & ICT

TREASURY MANAGEMENT MID-YEAR REPORT 2020-21
(CORPORATE SERVICES)

1 Purpose of the Report

To report on Treasury Management activities during the first half of 2020-21 (to 30 September 2020) and to indicate the Council's compliance with the prudential indicators set by Council at its meeting of 5 February 2020, in accordance with the Treasury Management in the Public Services: Code of Practice and Cross-Sectorial Guidance Notes 2017 (the Code).

2 Information and Analysis

(i) Introduction

Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Council to approve a Treasury Management Strategy before the start of each financial year and, as a minimum, a semi-annual and annual treasury outturn report. This report fulfils the Council's obligation under the CIPFA Code to produce a Treasury Management Mid-Year Report.

The Council's Treasury Management Strategy for 2020-21 was approved by Council on 5 February 2020, as part of the Capital Programme Approvals, Treasury Management and Capital Strategies Report. The Council has borrowed and invested substantial sums of money and is therefore potentially 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 is therefore central to the Council's Treasury Management Strategy.

(ii) External Context

Economy: The spread of the Covid-19 pandemic dominated during the period, as countries around the world tried to manage the delicate balancing act of containing transmission of the virus while easing lockdown measures and getting their populations and economies working again. Towards the end of the period agreement between the UK and EU on a Brexit trade deal was looking increasingly difficult.

The Bank of England (BoE) maintained its Bank Rate at 0.1% and its Quantitative Easing (QE) programme at £745 billion. The potential use of negative interest rates has not been discounted by BoE policymakers. The September 2020 Monetary Policy Committee meeting minutes commented that the Central Bank was having a harder look at its potential impact than was previously suggested and this surprised financial markets.

Government initiatives continued to support the economy, with the furlough (Coronavirus Job Retention) scheme keeping almost 10 million workers in jobs, grants and loans to businesses and 100 million discounted meals being claimed during the ‘Eat Out to Help Out’ (EOHO) offer.

Gross Domestic Product (GDP) growth contracted by 19.8% in the first quarter of the financial year (April to June 2020) according to the Office for National Statistics (ONS). This caused the annual growth rate to reduce further, to -21.5%. Recent monthly estimates of GDP have shown growth recovering, with the latest rise of almost 7% in July but even with the two previous monthly gains this still only makes up half of the lost output.

The headline rate of UK Consumer Price Inflation (CPI) fell to 0.2% year on year in August 2020, further below the BoE’s 2% target, with the largest downward contribution coming from restaurants and hotels influenced by the EOHO scheme. The ONS’ preferred measure of CPIH, which includes owner-occupied housing, was 0.5% year on year.

In the three months to July 2020, the unemployment rate increased from 3.9% to 4.1% while wages fell 1.8% for total pay in real terms (-0.7% for regular pay). Despite only a modest rise in unemployment over the period, the rate was expected to increase in the coming months, as the furlough scheme was due to end in October. On the back of this, the BoE forecast that unemployment could hit a peak of between 8% and 9%. However, the furlough scheme was extended to 31 March 2021, in an announcement on 5 November 2020, with a new national lockdown, for at least a month, announced on 31 October 2020.

The US economy contracted at an annualised rate of 31.7% in the first quarter of the financial year (April to June 2020). The Federal Reserve (Fed) maintained the Fed Funds rate at between 0% and 0.25% but announced a change to its inflation targeting regime. The move will allow the Central Bank to maintain interest rates at low levels for an extended period, to support the economy, even when inflation is ‘moderately’ above the 2% average target.

The European Central Bank (ECB) maintained its base rate at 0% and deposit rate at -0.5%.

Financial markets: Equity markets continued their recovery during the period, with the US Dow Jones climbing to not far off its pre-crisis peak, with the recovery being driven by a handful of technology stocks. The UK Financial Times Stock Exchange (FTSE) 100 and 250 have made up around half of their losses at the height of the first wave of the pandemic in March 2020. Central Bank and government stimulus packages continue to support asset prices, but volatility remains.

Very low interest rates and a move out of perceived less safe, to safer, investments continued, keeping gilts yields low but volatile over the period, with the yield on some short-dated UK Government bonds remaining negative. The 5-year UK benchmark gilt yield started and ended the June to September 2020 period at -0.06% (with much volatility in between). The 10-year gilt yield also moved significantly, starting at 0.21% and ending at 0.23% over the same period, while the 20-year gilt yield rose from 0.56% to 0.74%. 1-month, 3-month and 12-month bid rates averaged 0.02%, 0.06% and 0.23%, respectively over the period.

At the end of September 2020, the yield on 2-year US treasuries was around 0.13%, while that on 10-year US treasuries was 0.69%. German bund yields remained negative across most maturities.

Credit review: In the first quarter of the financial year there were many changes to the credit ratings of the financial institutions on the Council's counterparty list, however this reduced significantly in the second quarter.

There continues to be much uncertainty around the extent of the losses that banks and building societies will suffer due to the impact of the pandemic and for the UK institutions on the Council's list there is the added complication that the Brexit transition period ends on 31 December 2020 and a trade deal has yet to be agreed.

The institutions on the Council's external Treasury Management Advisor's counterparty list and recommended duration remain under constant review.

(iii) Local Context

On 31 March 2020, the Council had net borrowing of £103.094m arising from its revenue and capital income and expenditure. 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. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.20 Actual £m
General Fund CFR	525.169
Less: *Other debt liabilities	-68.878
Borrowing CFR	**456.291**
Less: Usable reserves	-305.525
Less: Working capital	-47.096
Net borrowing	**103.670**
Borrowing CFR is comprised:	
External borrowing	329.974
Internal borrowing	126.317
	456.291

** finance leases, PFI liabilities and transferred debt that form part of the Council's total debt*

The Council's strategy was to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk and keep interest costs low. The treasury management position as at 30 September 2020 and the in-year change is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.03.20 Balance £m	2020-21 Movement £m	30.09.20 Balance £m	30.09.20 Rate %
Long-term borrowing	277.474	-4.575	272.899	4.50
Short-term borrowing	52.500	104.000	156.500	0.31
Total borrowing	**329.974**	**99.425**	**429.399**	**2.98**
Long-term strategic pooled funds	59.892	1.812	61.704	3.73
Long-term investments	15.000	0.000	15.000	1.78
Short-term investments	82.912	152.088	235.000	1.23
Cash and cash equivalents	68.500	-36.764	31.736	0.06
Total investments	**226.304**	**117.136**	**343.440**	**1.58**
Net borrowing	**103.670**	**-17.711**	**85.959**	

Borrowing Activity

At 30 September 2020, the Council held £429.399m of loans, an increase of £99.425m, as part of its strategy for funding previous and current years' capital programmes. The mid-year borrowing position and the in-year change is shown in Table 3 below.

Table 3: Borrowing Position	31.03.20 Balance £m	2020-21 Movement £m	30.09.20 Balance £m	30.09.20 Interest Rate %	30.09.20 WAM* Years
Public Works Loan Board	262.474	-4.575	257.899	4.50	18
Banks (LOBO)	5.000	0.000	5.000	4.50	19
Banks (fixed-term)	10.000	0.000	10.000	4.69	24
Local authorities (long-term)	0.000	0.000	0.000	N/A	N/A
Local authorities (short-term)	52.500	104.000	156.500	0.31	0
Total borrowing	**329.974**	**99.425**	**429.399**	**2.98**	**18**

**WAM - Weighted Average Maturity*

The 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, with flexibility to renegotiate loans being a secondary objective, should the Council's long-term plans change.

In furtherance of these objectives, no new long-term borrowing was undertaken in the first half of 2020-21, while £4.575m of existing loans were allowed to mature without replacement. This strategy enabled the Council to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.

With short-term interest rates remaining much lower than long-term rates, the Council considers it to be more cost effective in the near term to use both internal resources and borrowed short-term loans instead. Additional short term borrowing has been secured in the six months to 30 September 2020 to finance the lump sum payment to the Derbyshire Pension Fund for the Council's employer contributions, in full, on 30 April 2020, for the period 1 April 2020 to 31 March 2021, with the intention to achieve a budget saving, originally approved by Cabinet on 16 March 2020, and amended by the Urgent Officer Decision made by Corporate Management Team Gold on 30 March 2020 and further reported to Cabinet on 23 April 2020; and to hold additional funding received by the D2N2 Local Enterprise Partnership (LEP), for which the Council is the accountable body. The net movement in short term loans is shown in Table 3 above.

The Council continues to hold £5.000m 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 Council has the option to either accept the new rate or to repay the loan at no additional cost. No banks exercised their option during the year.

Borrowing Update

On 9 October 2019 the Public Works Loan Board (PWLB) raised the cost of borrowing at the certainty rate to 1.8% above UK gilt yields, making it relatively expensive. Market alternatives are available; however the financial strength of individual authorities will be scrutinised by investors and commercial lenders.

The Chancellor's March 2020 Budget Statement included significant changes to PWLB policy and launched a wide-ranging consultation on the PWLB's future direction.

The consultation, titled "Future Lending Terms", allows stakeholders to contribute to developing a system whereby PWLB loans can be made available at improved margins to support qualifying projects. It contains proposals to allow authorities that are not involved in "debt for yield" activity to borrow at lower rates, as well as stopping local authorities using PWLB loans to buy commercial assets primarily for yield. The consultation also broaches the possibility of slowing, or stopping, individual authorities from borrowing large sums in specific circumstances.

The Council responded to the consultation which closed on 31 July 2020. The announcement and implementation of the revised lending terms is expected in the latter part of this calendar year or early next year.

The Municipal Bonds Agency (MBA) has revised its standard loan terms and framework agreement. Guarantees for the debt of other borrowers are now proportional and limited and a requirement to make contribution loans in the event of a default by a borrower has been introduced. The agency has issued 5-year floating rate and 40-year fixed rate bonds in 2020, in both instances Lancashire County Council is the sole borrower and guarantor.

If the Council intends future borrowing through the MBA, it will first ensure that it has thoroughly scrutinised the legal terms and conditions of the arrangement and is satisfied with them.

Other Debt Activity

After £4.104m repayment of prior years' Private Finance Initiative (PFI) contracts, finance leases and transferred debt liabilities, total debt other than borrowing stood at £68.878m on 30 September 2020, taking total debt to £498.277m.

Treasury Investment Activity

The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During the first half of 2020-21, the Council's investment balance ranged between £253.342m and £407.018m because of timing differences between income and expenditure. The year-end investment position and the year-on-year change is shown in Table 4 below.

Table 4: Investment Position (Treasury Investments)

	31.03.20 Balance £m	2020-21 Movement £m	30.09.20 Balance £m	30.09.20 Income Return %	30.09.20 Weighted Average Maturity days
Banks and building societies (unsecured)	37.402	-0.666	36.736	0.57	63
Government (including local authorities)	106.510	108.490	215.000	1.28	138
Registered Providers	5.000	0.000	5.000	2.15	513
Money Market Funds	17.500	7.500	25.000	0.08	0
Pooled Funds – Strategic Bond Funds	4.435	0.444	4.879	2.19	N/A
Pooled Funds – Equity Income Funds	10.267	0.616	10.883	4.37	N/A
Pooled Funds – Property Funds	23.243	-0.966	22.277	4.26	N/A
Pooled Funds – Multi Asset Income Funds	21.947	1.718	23.665	3.31	N/A
Total investments	**226.304**	**117.136**	**343.440**	**1.58**	**123**

**Weighted average maturity will apply to the first five categories above.*
Strategic *Pooled Funds have no maturity date but are realised when all units are sold.*

Both the CIPFA Code and Government guidance require the 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 Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

In the light of the pandemic crisis and the likelihood of unexpected calls on cash flow, the Council kept more cash available at very short notice than is normal. Liquid cash was diversified over several Money Market Funds, to manage both credit and liquidity risks.

On 25 September 2020, the overnight, 1 and 2-week deposit rates on Debt Management Account Deposit Facility (DMADF) deposits dropped below zero percent, to -0.03%, the rate was 0% for 3-week deposits and 0.01% for longer maturities.

The return on Money Market Funds, net of fees, also fell over the six months and for many funds net returns ranged between 0% and 0.1%. In many instances, the fund management companies have temporarily lowered or waived fees to maintain a positive net return.

Given the increasing risk and low returns from short-term unsecured bank investments, the Council diversified into higher yielding asset classes, as shown in Table 4 above. As a result, an additional 0.48% has been added on to total income return in 2020-21 and investment risk remains diversified.

The progression of credit risk and return metrics for the Council's investments managed in-house are shown in the extracts from the Council's external investment advisor's (Arlingclose) quarterly investment benchmarking in Table 5 below.

Table 5: Investment Benchmarking – Treasury investments managed in-house

	Credit Score	**Credit Rating**	**Bail-in Exposure**	**Weighted Average Maturity (days)**	**Rate of Return %**
31.3.2020	4.15	AA-	33%	110	-1.11
30.9.2020	4.11	AA-	22%	135	0.00
Similar Local Authorities	3.87	AA-	49%	991	-0.37
All Local Authorities	4.16	AA-	64%	18	-0.46

At 30 September 2020, the Council's portfolio of externally managed pooled strategic bond, equity income, property and multi-asset funds amounted to £61.704m. The Council holds these funds with the aim of receiving regular revenue income and because over the long-term their prices are relatively stable.

In the relatively short period since the onset of the Covid-19 pandemic in March 2020 and the ensuing enforced lockdown in many jurisdictions, the global economic fallout has been sharp and large. Market reaction was extreme, with large falls in equities, corporate bond markets and, to some extent, real estate, echoing lockdown-induced paralysis and the uncharted challenges for governments, business and individuals.

The Council is invested in bond, equity, multi-asset and property funds. The falls in the capital values of the underlying assets, in particular bonds and equities, were reflected in 31 March 2020 fund valuations, with all funds registering negative capital returns over a 12-month period. Since March 2020 there has been an improvement in market sentiment, which is reflected in an increase in capital values of the strategic bond and multi-asset income funds and all of the equity income funds in the Council's portfolio. However, the capital value of the property fund is below its value at 31 March 2020. Market values at 31 March 2020 and 30 September 2020 are as shown in Table 4, above.

Similar to many other property funds, dealing (i.e. the buying, or selling, of units) in the CCLA Local Authorities Property Fund was suspended by the fund in March 2020. The relative infrequency of property transactions in March 2020, as the pandemic intensified, meant that it was not possible for valuers to be confident that their valuations correctly reflected prevailing conditions. To avoid the material risk of disadvantage to buyers, sellers and holders of units in the property fund, the management company was obliged to suspend transactions until the required level of certainty was re-established. The dealing suspension was lifted in September 2020. There has also been a change to redemption terms for the CCLA Local Authorities Property Fund; from September 2020 investors are required to give at least 90 calendar days' notice for redemptions.

During the first half of 2020-21 these funds have generated £1.216m of income, which is being used to support services in 2020-21, and a recovery of £1.812m of the unrealised capital loss of £9.532m at 31 March 2020. These pooled funds have no defined maturity date but are available for withdrawal after a notice period. Their performance and continued suitability in meeting the Council's investment objectives are regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down over months, quarters and even years; but with the confidence that over a three to five-year period total returns will exceed cash interest rates. The Council is using the alternative fair value through profit and loss (FVPL) accounting method to account for these funds, which means that if there are any long term unrealised losses in the funds' fair values there will not be an impact on the Council's General Reserve balance until 2023-24 at the earliest. In light of their performance over the medium-term and the Council's latest cash flow forecasts, investment in these funds has been maintained during the first half of 2020-21 (see Table 4).

Non-Treasury Investments

The definition of investments in CIPFA's revised Treasury Management Code covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. This is replicated in the Ministry of Housing, Communities and Local Government's (MHCLG) Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return. This includes service investments for operational and/or regeneration, as well as commercial investments which are made mainly for financial reasons.

At 30 September 2020, the Council held £13.113m of investments in loans to local businesses and community trusts:

- £12.613m regeneration loan - Buxton Crescent Hotel Limited
- £0.500m loan to communities - Chesterfield Football Club Community Trust.

This represents an increase of £0.845m on the balance at 31 March 2020 because of a further investment of £0.345m in the Buxton Crescent Hotel Limited and a new investment of £0.500m in the Chesterfield Football Club Community Trust.

These investments generated £0.345m in interest and fees for the Council in first half of 2020-21, after taking account of direct costs, representing a rate of return of 5.51%.

Treasury Performance

The Council measures the financial performance of its treasury management activities both in terms of its impact on the revenue budget and its relationship to benchmark interest rates, as shown in Table 6 below. Investment benchmarking is performed quarterly and debt benchmarking is performed annually.

Table 6: Performance

	30.09.20 Actual £m	30.09.20 (CFR) Budget £m	Over/ (Under) £m	Interest Actual %	Interest Other LA Benchmark %	Interest Over/ (Under) %
Borrowing	5.515	9.213	(3.698)	4.30	3.42	0.88
Investments	4.140	3.125	1.015	0.02	-0.32	0.34

The Council's average interest rate on long term borrowing is higher than the Other Local Authority Benchmark because the majority of the Council's borrowing was taken out at the higher rates prevalent prior to the financial crisis of 2008-09. The Council's policy has been to utilise its internal reserves rather than take additional external borrowing thus saving interest payments totalling millions of pounds.

The Council surpassed its first half 2020-21 net investment income (gross investment income less short-term borrowing costs) target of £3.125m by 30 September 2020.

Estimates for Income in 2020-21

The corporate world is still adjusting to the economic shock as a result of the pandemic, with probably more to come, and it is still too early to tell which companies will withstand the economic damage in the short to medium-term, or which will choose to conserve cash in very difficult economic conditions simply to survive.

Investment income in the Council's 2020-21 Revenue Budget was set against a very different economic backdrop. The BoE Bank Rate, which was 0.75% in January/February 2020, now stands at 0.10%. Interest earned from short-dated money market investments is also significantly lower. In relation to income from the Council's externally managed strategic funds, dividends and income distributions will ultimately depend on many factors, including, but not limited to, the duration of the pandemic and the extent of its economic impact, the fund's asset allocation in different sectors, securities held/bought/sold and, in the case of equities, enforced or voluntary dividend cuts or deferral.

Following guidance from the Council's external Treasury Management Advisors, the Council has reviewed its expectations for investment income in 2020-21 and has made downward adjustments as follows:

- Bond funds and property funds: 20% lower
- Multi-asset income funds: 25% lower
- Equity income funds: 50% lower

and will monitor and report on actual income received during the year.

Compliance Report

The Director of Finance & ICT reports that all treasury management activities undertaken during the first half of 2020-21 complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy.

Compliance with the authorised limit and operational boundary for external debt is demonstrated in Table 7 below and compliance with specific investment limits is demonstrated in Table 8 below.

Table 7: Debt Limits

	Half Year Maximum £m	30.09.20 Actual £m	2020-21 Operational Boundary £m	2020-21 Authorised Limit £m	Complied
Short Term Borrowing	156.500	156.500	N/A	160.000	✓
Long Term Borrowing	277.474	272.899	N/A	N/A	N/A
PFI and Finance Leases	68.878	68.878	N/A	N/A	N/A
Total debt	**502.852**	**498.277**	**816.000**	**847.000**	✓

Table 8: Investment Limits

	Half Year Maximum £m	30.09.20 Actual £m	2020-21 Limit £m	Complied
Any single organisation, except UK Central Government (Lloyds Bank (Main Bank) includes additional £30m Operational Limit)	57.440	30.000	60.000	✓
Any group of organisations under the same ownership (Lloyds Bank – as above)	57.440	30.000	60.000	✓
Any group of pooled funds under the same management (Money Market Funds)	30.000	25.000	30.000	✓
Registered providers	5.000	5.000	50.000	✓
Money Market Funds – Total	112.500	25.000	300.000	✓
Non-Treasury Investments (loans to unrated bodies)	13.113	13.113	13.113	✓
Non-Specified investments (Local Authority Loans > 365 days, Strategic Pooled Funds & Non-Treasury Loans)	77.761	77.054	150.000	✓

Treasury Management Indicators

The Council measures and manages its exposure to treasury management risks using the following indicators.

Security: The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating 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.

	30.09.20 Actual	2020-21 Target	Complied
Portfolio average credit rating	AA-	A	✓

Liquidity: The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available within a rolling three-month period and additional borrowing secured without giving prior notice.

	30.09.20 Actual £m	2020-21 Target £m	Complied
Total cash available within 3 months	141.736	30.000	✓
OR			
Total sum borrowed in past 3 months without prior notice	113.000	30.000	✓

Interest Rate Exposures: This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of net principal borrowed were:

	31.03.20 Actual %	2020-21 Limit %	Complied
Upper limit on fixed interest rate exposure	62	100	✓
Upper limit on variable interest rate exposure	38	40	✓

Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year, or the transaction date if later. All other instruments are classed as variable rate.

Maturity Structure of Borrowing: This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of all borrowing were:

	30.09.20 Actual %	Upper Limit %	Lower Limit %	Complied
Under 12 months	38	40	0	✓
12 - 24 months	0	20	0	✓
24 months - 5 years	4	20	0	✓
5 - 10 years	8	20	0	✓
10 - 20 years	23	40	10	✓
20 - 30 years	20	40	10	✓
Over 30 years	7	40	0	✓

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

Principal Sums Invested for Periods Longer than 365 days: The purpose of this indicator is to control the 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:

	Beyond 30.09.21 £m	Beyond 30.09.22 £m	Beyond 30.09.23 £m
Strategic Pooled Funds	61.704	61.704	61.704
Long Term Deposits	28.113	13.113	13.113
Total Invested	**89.817**	**74.817**	**74.817**
Limit on Long Term Funds	**150.000**	**125.000**	**100.000**
Complied	✓	✓	✓

Other

The implementation of the new IFRS 16 Leases accounting standard has been delayed until 2021-22.

The medium-term global economic outlook is weak. While the strict initial lockdown restrictions had eased, Covid-19 has not been supressed and second waves have prompted more restrictive measures on a regional, then national basis from 5 November 2020. This ebb and flow of restrictions on normal activity will continue for the foreseeable future, at least until an effective vaccine is produced and importantly, distributed.

The global Central Bank and government responses have been significant and are in many cases on-going, maintaining more stable financial, economic and social conditions than otherwise. This supported a sizeable economic recovery in the third quarter of 2020.

However, the scale of the economic shock to demand, on-going social distancing measures, regional lockdowns and reduced fiscal support will mean that the subsequent pace of recovery is limited. Early signs of this are already evident in UK monthly GDP and Purchasing Managers Index (PMI) data, even before the latest restrictions.

This situation will result in central banks maintaining low interest rates for the medium term. In the UK, Brexit is a further complication. BoE Bank Rate is therefore likely to remain at low levels for a very long time, with a distinct possibility of being cut to zero. Money markets have priced in a chance of a negative Bank Rate.

Longer-term yields will also remain depressed, anchored by low central bank policy rates, expectations for potentially even lower rates and insipid inflation expectations. There is a chance that yields may follow a slightly different path in the medium term, depending on investor perceptions of growth and inflation, or if the UK leaves the EU without a deal.

The Council's external Treasury Management Advisor expects BoE Bank Rate to remain at the current 0.10% level and additional monetary loosening in the future, most likely through further financial asset purchases (QE). While their central case for BoE Bank Rate is no change from the current level of 0.10%, further cuts to BoE Bank Rate to zero, or even into negative territory, cannot be completely ruled out.

Gilt yields are expected to remain very low in the medium term. Shorter-term gilt yields are currently negative and will remain around zero, or below, until either the BoE expressly rules out negative Bank Rate, or growth/inflation prospects improve.

Downside risks remain in the near term, as the Government attempts to dials down its fiscal support measures, reacts to the risk of a further escalation in infection rates and the Brexit transition period comes to an end.

3 Considerations

In preparing this report the relevance of the following factors has been considered:- financial, legal, prevention of crime and disorder, equality and diversity, human resources, environmental, health, property, transport and social value considerations.

4 Background Papers

Treasury Management Strategy 2020-21.

Papers held electronically by Technical Section, Finance & ICT Division.

5 Key Decision

No

6 Is it necessary to waive the call-in period?

No

7 Officer's Recommendation

That Cabinet notes the Treasury Management Mid-Year Report 2020-21 and notes the Council's compliance to date with the prudential indicators set by Council for 2020-21, in accordance with the terms of the Treasury Management in the Public Services: Code of Practice and Cross-Sectorial Guidance Notes 2017.

PETER HANDFORD

Director of Finance & ICT