OFFICE OF THE POLICE & CRIME COMMISSIONER OFFICE OF THE CHIEF CONSTABLE	
TITLE:	**Treasury Management Annual Report 2020/21**
DATE:	**10th June 2021**
TIMING:	**Routine**
PURPOSE:	**For consideration**

1.	**RECOMMENDATION**
1.1	That the Annual Treasury Management Activity Report and actual Prudential Indicators for 2020/21 are approved.
2.	**INTRODUCTION & BACKGROUND**
2.1	Treasury Management is the management of cash flows, banking, money market and capital market transactions and the management of the associated risks, in the pursuit of the optimum performance or return consistent with those risks.
2.2	The Treasury Management Annual Report is a requirement of the Police and Crime Commissioner's (PCC's) statutory reporting responsibilities.
2.3	The report meets the requirements of both the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities. The PCC is required to comply with both Codes through Regulations issued under the Local Government Act 2003.
2.4	The report covers both Treasury Management activity during 2020/21 and the actual Prudential Indicators for 2020/21.
2.5	During 2020/21, the minimum reporting requirements were that the PCC received an annual treasury management strategy in advance of the year, a mid-year update report and an annual report following the year end, describing the actual performance or activity compared to the annual strategy.
3.	**ISSUES FOR CONSIDERATION**
3.1	**Capital Expenditure and Financing**
3.1.1	During each financial year the PCC incurs expenditure on acquiring and enhancing land, buildings, vehicles and other long-term assets. These activities are known as capital expenditure. Such expenditure may either be: a) Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on borrowing need; or b) If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

3.1.2 Actual capital expenditure forms one of the required Prudential Indicators. The table below shows capital expenditure in the respective years and how this was financed. The 2020/21 Estimate of Capital expenditure is as per the Treasury Management Strategy for 2020/21.

	2019/20 Actual £m's	2020/21 Estimate £m's	2020/21 Actual £m's
Capital Expenditure	**9.932**	**28.063**	**15.969**
Financed by:			
Capital Receipts	0.000	0.000	0.000
Capital Grants and PIF Grants	0.459	0.539	0.121
Reserves	6.578	24.879	8.951
Revenue	2.895	2.645	6.897
Unfinanced Capital Expenditure	**0**	**0**	**0**

3.2 Borrowing Requirement

3.2.1 The PCC's underlying need to borrow is called the Capital Financing Requirement (CFR). This figure is a gauge of the PCC's debt position. It represents 2020/21 and any prior years' capital expenditure which has not yet been financed by revenue or other resources.

3.2.2 Part of the PCC's treasury activity is to address this borrowing need, either through borrowing from external bodies, or utilising temporary internal cash resources.

3.2.3 Under treasury management arrangements, actual debt can be borrowed or repaid at any time within the confines of the annual Treasury Management Strategy. However, the PCC is required to make an annual revenue charge to reduce the CFR. This statutory revenue charge is called the Minimum Revenue Provision (MRP). The total CFR can also be reduced by:

a) The application of additional capital resources; or

b) Charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

3.2.4 The PCC's CFR for the year is shown below and represents a key prudential indicator.

	2019/20 Actual £m	2020/21 Estimate £m	2020/21 Actual £m
Capital Financing Requirement	0	0	0

3.3	**Treasury Position**
3.3.1	Whilst the PCC's gauge of his underlying need to borrow is the CFR, the Chief Finance Officer for the PCC can manage the actual borrowing position by either: a) Borrowing to the CFR amount; b) Choosing to utilise some temporary internal cash flow funds in lieu of borrowing (under-borrowing); or c) Borrowing for potential future increases in the CFR (borrowing in advance of need).
3.3.2	The figures in this report are based on the carrying amounts borrowed and invested and therefore reflect those figures disclosed in the Statement of Accounts.
3.3.3	The treasury position at the 31st March 2021 compared with previous year comparators was:

	31st March 2020		31st March 2021	
	Principal £m	Average Interest Rate %	Principal £m	Average Interest Rate %
Actual Borrowing Position				
Fixed Rate Debt	0	0	0	0
Variable Rate Debt	0	0	0	0
Total Debt	0	0	0	0
Underlying Borrowing Requirement (excl. PFI)	0		0	
(Over) / Under Borrowing	0		0	
Actual Investment Position				
Fixed Interest Investments	38.122	0.9	31.081	0.39
Variable Interest Investments	3.500	0.5	5.000	0.02
Total Investments	41.622		36.081	
Cash & Cash Equivalents	3.608		6.239	
Net Borrowing	(45.230)		(42.320)	

3.4	**Prudential Indicators and Compliance Issues**
3.4.1	Some of the Prudential Indicators provide either an overview or specific limits on treasury activity and these are shown below:
3.4.2	Gross Borrowing and the CFR In order to ensure that borrowing levels are prudent over the medium term, the PCC's borrowing must only be for a capital purpose. Gross borrowing should not therefore, except in the short term, have exceeded the CFR for 2020/21 plus the expected changes to the CFR over 2021/22 and 2022/23 etc.

The table below highlights the PCC's gross borrowing position against the CFR.

	2019/20 Actual £m	2020/21 Estimate £m	2020/21 Actual £m
Gross Borrowing (incl. PFI)	0	0	0
External Borrowing (excl. PFI)	0	0	0
Capital Financing Requirement (CFR)	0	0	0

3.4.3 The above table shows that gross debt is exactly the same as the CFR and therefore this prudential indicator has been met and reflects the Commissioner's decision to repay all external borrowing during 2016/17 and the termination of the PFI contract.

3.4.4 The Authorised Limit

The Authorised Limit is the 'Affordable Borrowing Limit' required by Section 3 of the Local Government Act 2003. The PCC does not have the power to borrow above this level.

The table below demonstrates that during 2020/21 the PCC maintained gross borrowing within the Authorised Limit.

3.4.5 The Operational Boundary

The Operational Boundary is the expected borrowing position during the year. Periods where the actual position is either below or over the Operational Boundary are acceptable subject to the Authorised Limit not being breached.

3.4.6 Maximum Gross Borrowing

This is the Gross Borrowing at the beginning of the financial year.

3.4.7 Average Gross Borrowing

This is the average of the borrowing position at the beginning of the year and the borrowing position at the end of the year.

	2020/21 £m
Authorised Borrowing Limit	6,220
Operational Boundary	0
Actual Maximum Gross Borrowing Position	0
Average Gross Borrowing Position	0
Estimated Financing Costs as a % of Net Revenue Stream	(0.18%)
Actual Financing Costs as a % of Net Revenue Stream	(0.19%)

3.4.8 Actual financing costs as a proportion of Net Revenue Stream (NRS)

This indicator identifies the trend in the cost of capital (borrowing and other long-term obligation costs) against the Net Revenue Stream (NRS). For the calculation, NRS equals the Revenue Budget for the year of £138.991m.

	Actual Financing costs as a % of NRS is a negative as all external debt was settled in 2016/17, so only investment income is included. The actual percentage is higher than the estimated value due to slippage of capital programme schemes into 2021/22 and beyond. In addition, the actual interest rate received on investments was higher than forecast.
3.4.9	On the 23rd March 2021 there was a breach in the current bank account, due to the fault of Thurrock Council not repaying a £3m loan on the day it was due. Thurrock Council admitted its liability and were charged the overdraft fees for this breach and were reminded about timely repayment. The internal process has been reviewed and it is planned to introduce a 10 a.m. deadline, whereby the finance officers will contact the counterparties if cash has not arrived in the Commissioner's bank account. There will also be a workshop to further review the current process and share the experience of the more experienced members of staff.
3.5	**Economic Background and Interest Rates**
3.5.1	The 2020/21 financial year was dominated by the Coronavirus pandemic and the damage that it did to world economies through lockdowns. This led Central Banks around the world to take emergency action in March 2020 to support economies, by reducing central rates to near zero or further into negative territory; and to embark on quantitative easing.
3.5.2	Governments also took major fiscal action to stimulate their economies and to protect jobs from being lost. In the UK, the Bank of England cut Bank Rate from 0.75% first, to 0.25% and then to 0.10% in March 2020. It definitively ruled out using a negative Bank Rate at its February 2021 meeting, at least during the current downturn. The Federal Reserve in the US also cut the Federal Rate to near zero, while the European Central Bank called a halt at (0.50%). The net result was that gilt yields fell to historically low levels, indeed as late as 31st December 2020 all gilt yields from 1 to 8 years were negative.
3.5.3	The US and UK have followed similar paths during this year and have both made rapid progress during the spring of 2021 with rolling out vaccines and getting a high take up, so that around half of all adults had received one vaccination by the end of March 2021. This will enable a rapid easing of restrictions on the economy and personal life. In addition, fiscal action by both Governments has poured support into the economy. In the US, a $900bn fiscal support package in December 2020 was followed by a $1.9trn (8.8% of GDP) stimulus package in March 2021. In the UK, the March 2021 Budget provided yet another round of economic support. In addition, there has been a significant shift in the policy for implementing Central Bank's mandates on inflation and full employment in 2020/21. The Federal Reserve agreed at its September 2020 meeting to target average inflation of 2%; meaning that it would tolerate inflation rising above 2% for periods, in order to offset periods when it was running below 2%. The Bank of England adopted a similar policy at its 5th November 2020 meeting. Gilt yields first started a sharp rise in the UK after the 5th February 2021 Monetary Policy Meeting (which ruled out using a negative Bank Rate). However, the rapidly improving economic outlook during the final two months of 2020/21 stoked concerns in financial markets in the UK and the US, that both Central Banks would have to raise central rates quicker than previously expected and also led to bond yields rising to allow for higher expected rates of inflation. Neither Central Bank made any comments

	that they would take action to suppress the sharp rise in bond yields, especially in medium and long-term yields.
3.5.4	The story has been very different in the EU, with both the roll out and take up of vaccines being disappointingly slow at a time during March 2021, when many countries were experiencing a sharp rise in cases. This rise has threatened to overwhelm hospitals in some major countries and has led to renewed severe restrictions or lockdowns during March 2021. This will inevitably put back economic recovery and a return to pre-pandemic levels is not expected now until the second half of 2022. Bond yields in the EU have therefore not risen as sharply as in the US and the UK.
3.5.5	As for investment rates, short term rates plunged after the Bank Rate was cut to 0.10% in March 2020. Six-month to one-year rates progressively declined during the year until nearly all rates were around, or marginally below zero by 31st December 2020 - since then they have risen marginally. As for equity markets, the FTSE 100 plunged to a low of just under 5,000 in March 2020. Since then it has gradually recovered to end at 6,713 at the 31st March 2021.
3.6	**Investment Position**
3.6.1	Investment Policy – The PCC's investment policy is governed by the Welsh Government, which has been implemented in the annual investment strategy.
3.6.2	Resources – The PCC's longer-term cash balances comprise primarily of revenue and capital resources, although these will be influenced by cash flow considerations. The PCC's core cash resources were comprised as follows; and these represent the total funds available for investment:

	2019/20 £m	2020/21 £m
General Reserves	4.000	4.000
Earmarked Reserves	39.609	35.310
Provisions	1.417	1.537
Useable Capital Receipts	2.498	2.498
Total	47.524	43.345

3.6.3	Investments Held by the PCC - The PCC concluded the year with a balance of £36.081m of internally managed funds, which compares with a budget assumption of £25.972m as per the annual Treasury Management Strategy. The difference between the budget and actual position is explained by slippage of capital programme schemes into 2020/21 and beyond (particularly in relation to the replacement of HQ) and in-year savings against budget which has resulted in surplus funds available for investment purposes.
3.6.4	These internally managed funds received an average return of 0.64% compared to a budget assumption of 0.60%. The comparable performance indicator is the average 7-day LIBID rate, which was 0.04%. The budget assumption of 0.60% average return reflected a different mix of investments between fixed and variable deposits.
3.7	**Regulatory Framework, Risk and Performance**

3.7.1	The PCC's treasury management activities are regulated by a variety of professional codes, statutes and guidance: a) CIPFA's Treasury Management Code of Practice (2017 Edition); b) CIPFA Guide for Chief Financial Officers on Treasury Management in Local Authorities; c) CIPFA Standard of Professional Practice on Treasury Management; d) The Prudential Code for Capital Finance in Local Authorities (2017 Edition); e) Local Government Act 2003; f) Bank of England Non-Investment Products Code (2011); g) Standing Orders relating to Contracts; h) Financial Standing Orders, Regulations and Procedures; i) The Commissioner's Manual of Corporate Governance and Scheme of Delegation; and j) Markets in Financial Instruments Directive (MiFiD II).
3.7.2	The PCC complied with all of the above relevant statutory and regulatory requirements which require the PCC to identify and, where possible, quantify the levels of risk associated with his treasury management activities. In particular his adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that his capital expenditure is prudent, affordable and sustainable; and his treasury practices demonstrate a low risk approach.
4.	**<u>NEXT STEPS</u>**
4.1	A Treasury Management update report, reviewing performance for the first six months of 2021/22 will be presented to the Joint Audit Committee in December 2021.
5.	**<u>FINANCIAL CONSIDERATIONS</u>**
5.1	These are detailed in the report.
6.	**<u>PERSONNEL CONSIDERATIONS</u>**
6.1	There are no staffing/personnel implications arising from this report.
7.	**<u>LEGAL IMPLICATIONS</u>**
7.1	There are no legal implications arising from this report.
8.	**<u>EQUALITIES AND HUMAN RIGHTS CONSIDERATIONS</u>**
8.1	This proposal has been considered against the general duty to promote equality, as stipulated under the Strategic Equality Plan and has been assessed not to discriminate against any particular group.
8.2	In preparing this report, consideration has been given to the requirements of the Articles contained in the European Convention on Human Rights and the Human Rights Act 1998.
9.	**<u>RISK</u>**
9.1	Treasury management can never be risk free. In borrowing, the risk is that the PCC incurs a higher interest charge than was necessary and in lending

	there is the risk of default on repayment and the risk that a better rate of interest could have been achieved from an alternative borrower with acceptable credit status. Adherence to the CIPFA Code of Practice on Treasury Management is best practice in terms of balancing risk and return.
10.	**PUBLIC INTEREST**
10.1	This is a public document.
11.	**CONTACT OFFICER**
11.1	Darren Garwood-Pask, Chief Finance Officer.
12.	**ANNEXES**
12.1	None.