Appendix A

NORTHUMBRIA POLICE AND CRIME COMMISSIONER

Key Decision

Treasury Management Annual Report 2021/22

(PCC/478/2022)

Summary

The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (the Code) requires the Commissioner to receive a Treasury Management Annual Report on borrowing and investment activity each year.

This report meets this requirement and informs the Commissioner of Treasury Management activity during 2021/22.

The report was reviewed by the Joint Independent Audit Committee at their meeting on 26 September 2022.

Recommendation

Approve the Treasury Management Annual Report as a true record of the activities for 2021/22, and publish it on the Commissioners website

Northumbria Police and Crime Commissioner

I hereby approve the recommendation above.

Signature **Date 27.10.2022**

Appendix A

OPCC SCRUTINY MEETING	**03 OCTOBER 2022**
TREASURY MANAGEMENT ANNUAL REPORT 2021/22	
REPORT OF: THE JOINT CHIEF FINANCE OFFICER	
AUTHOR: GAIL THOMPSON, T/HEAD OF FINANCE	

1. PURPOSE

1.1 In-line with the Code of Practice on Treasury Management this report presents to the Police and Crime Commissioner (the Commissioner) the Treasury Management Annual Report for the financial year 2021/22, for review and acceptance.

2. RECOMMENDATION

2.1 The Commissioner is recommended to:

a) Review the attached Treasury Management Annual Report 2021/22; and

b) Approve the Treasury Management Annual Report as a true record of the activities for 2021/22 and publish it on the Commissioners website.

3. BACKGROUND

3.1 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (the Code) requires the Commissioner to receive a Treasury Management Annual Report on borrowing and investment activity each year. This report meets that requirement and informs the Commissioner of Treasury Management activity during 2021/22.

3.2 In-line with good governance principles included within the Code, the attached Treasury Management Annual Report has been presented and reviewed by the Joint Independent Audit Committee on 26 September 2022.

4 KEY OUTCOMES

4.1 The Treasury Management Annual Report 2021/22 is attached at Appendix A. The key highlights are as follows:

- Investment income was £0.034m higher than budgeted reflecting additional cash and reserve balances available for investment and the accelerated increase in Bank Rate over the year. Whilst the budget assumed Bank Rate would remain flat at 0.10%, the Bank of England increased Bank Rate to 0.25% in December 2021 with further increases to 0.50% in February 2022 and 0.75% in March 2022.

- Borrowing costs were £0.129m less than the original budget estimate, reflecting increased reserve balances available for internal borrowing and a lower borrowing requirement for capital financing.

- Financial Regulations have been complied with and all Prudential Indicators were within the limits set for the year within the Treasury Management Strategy. There were two short-term counterparty breaches that were corrected the following working day and posed no material risk to the Commissioner's funds.

5. CONSIDERATIONS

Freedom of Information	*Non-exempt*
Consultation	Yes
Resource	No
There are no additional financial considerations arising from this report.	
Equality	No
There are no equality implications arising from the content of this report.	
Legal	No
There are no legal considerations arising from the content of this report.	
Risk	No
There are no additional risk management implications directly arising from this report.	
Communication	Yes
To be reported to the PCC in-line with The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (the Code) by 30 September each year.	
Evaluation	No

6 Treasury Management Annual Report 2021/22

The Strategy for 2021/22

1. The 2021/22 Treasury Management Policy Statement and Strategy was approved by the Joint Independent Audit Committee (JIAC) on 22 February 2021 for presentation to the Police and Crime Commissioner (PCC). The key decision was approved by the PCC on 9 March 2021.

2. The formulation of the 2021/22 Treasury Management Strategy involved determining the appropriate borrowing and investment decisions with the prime objective of safeguarding assets and secondary objectives of managing liquidity, obtaining a reasonable rate of return on investments and minimising the costs of borrowing.

3. The Treasury Management Strategy fully complied with the requirements of The Chartered Institute of Public Finance and Accountancy Code of Practice on Treasury Management and covered the following:

   - Prospects for interest rates.
   - Treasury limits set for prudential indicators.
   - The investment strategy.
   - The borrowing strategy.

Investment Strategy

4. Investments are managed in-house using counterparties listed in an approved lending list consistent with the agreed Treasury Management Strategy. Investments are placed over a range of periods and are dependent on the assessed security of the counterparty, the liquidity requirements of the cash flow, actual interest rates and expectations of movements in interest rates.

5. The expectation for interest rates within the Treasury Management Strategy for 2021/22 anticipated Bank Rate to remain unchanged at 0.10% through to March 2022 and beyond. The Strategy noted that the coronavirus outbreak had caused significant economic damage to the UK and economies around the world. No increase in Bank Rate was expected in the near-term, as at the time it was thought unlikely that inflation would rise sustainably above 2% during this period, so as to warrant increasing Bank Rate.

6. The Treasury Management Strategy was to adopt caution in the management of the 2021/22 treasury operations. The interest rate market was monitored to allow the Chief Finance Officer (CFO) to adopt a pragmatic approach to any changing circumstances, having delegated powers to invest and manage the funds and monies of the PCC.

Borrowing Strategy

7. The borrowing strategy for 2021/22 was:

   - Consider the use of short-term borrowing as a bridge until capital receipts are received.
   - Consider the use of market loans which are at least 20 basis points below the PWLB target rate, where they become available.

- Consider, where required, the use of PWLB loans where rates fall below Link Group trigger rates, with preference given to terms which ensure a balanced profile of debt maturity.

- Consider the use of reserve and General Fund balances to limit the requirement for new borrowing, reducing investment balances rather than increasing external borrowing in order to minimise interest costs.

- Maintain a flexible strategy in order to allow decisions on borrowing to be taken which balance the refinancing risk associated with an increase in interest rates against any potential short-term savings.

8. The early repayment of debt was not considered to present value for money during 2021/22, as the cost of premiums payable on the early repayment of debt continue to outweigh any potential savings on refinancing.

Treasury Management Compliance with Risk Strategy

9. The primary objective is to ensure the security of funds and minimise risks, including counterparty and interest rate risks. In January 2022 the Internal Audit report on the review of the treasury management function gave the opinion that it was 'Operating Well'.

Outturn 2021/22 – Performance Measurement

10. Prudential indicators are set annually to ensure that borrowing is prudent, sustainable and affordable. Performance is monitored against these indicators throughout the year and reported in the quarterly capital monitoring reports to the Joint Business Meeting (JBM). The outturn against the prudential indicators confirms that all indicators were operating within agreed limits. A copy of the prudential indicators is attached at Appendix 1.

11. There were two short-term counterparty breaches during the year that were corrected the following working day and posed no material risk to the PCC's funds:

Date	Counter Party / Limit	Reason for the Breach
6 August 2021	Handelsbanken Bank Limit - lower of £20.000m or 20% of available investment balance	Error in the calculation of the 20% available balance led to an investment balance of £19.158m instead of a maximum of £17.778m. This was corrected on the following working day. Handelsbanken is a high rated bank and the balance invested was within the absolute limit of £20m for investments.
5 January 2022	Barclays Bank Limit - £10.000m	The treasury assessment on the morning of 5 January did not take into account the scheduled return of an investment balance of £10.000m. The income hit the account late in the afternoon after the balance was checked against the treasury assessment taking the Barclays current account to a total of £10.208m. This was corrected on the following working day.

External Advisers

12. Link Group have continued to be used as external treasury management advisers to assist in achieving the objectives set out in the Treasury Policy Statement and Strategy and provide access to specialist skills and resources.

Investment strategy and control of interest rate risk

13. Investment returns remained close to zero for much of 2021/22. The expectation for interest rates within the treasury management strategy for 2021/22 was that Bank Rate would remain at 0.1% for the full year and would not be increased until it was clear to the Bank of England that the emergency level of rates introduced at the start of the Covid-19 pandemic were no longer necessitated.

14. The Bank of England and the Government also maintained various monetary and fiscal measures, supplying the banking system and the economy with massive amounts of cheap credit so that banks could help cash-starved businesses to survive the various lockdowns/negative impact on their cashflow. The Government also supplied huge amounts of finance to local authorities to pass on to businesses. This meant that for most of the year there was much more liquidity in financial markets than there was demand to borrow, with the consequent effect that investment earnings rates remained low until towards the turn of the year when inflation concerns indicated central banks, not just the Bank of England, would need to lift interest rates to combat the second-round effects of growing levels of inflation (CPI was 6.2% in February).

15. The PCC does not have sufficient cash balances to be able to place deposits longer term so cannot benefit from the higher rates that these longer types of investments attract.

16. Whilst the PCC has taken a cautious approach to investing, there is also an appreciation of the changes to regulatory requirements for financial institutions, in terms of additional capital and liquidity, that came about in the aftermath of the financial crisis. These requirements have provided a far stronger basis for financial institutions. Annual stress tests by regulators have evidenced how institutions are now far more able to cope with extreme stressed market and economic conditions.

17. Investment balances have been kept to a minimum through the agreed strategy of using reserves and balances to support internal borrowing, rather than borrowing externally from the financial markets. External borrowing would have incurred an additional cost, due to the differential between borrowing and investment rates. Such an approach has also provided benefits in terms of reducing the counterparty risk exposure, by having fewer investments placed in the financial markets.

Borrowing strategy and control of interest rate risk

18. During 2021/22, the PCC maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt as cash supporting the PCC's reserves, balances and cash flow was used as an interim measure. This strategy was prudent as investment returns were very low and counterparty risk on the placing of investments was minimised.

19. A cost of carry can remain during the year on any new long-term borrowing that is not immediately used to finance capital expenditure, as it can cause a temporary increase in cash balances; this would then incur a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns. There was no new long-term borrowing taken during 2021/22 and therefore this risk was nil.

20. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this was kept under review to avoid incurring higher

borrowing costs in the future when this authority may not be able to avoid new borrowing to finance capital expenditure and/or the refinancing of maturing debt.

21. Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. The Director of Finance therefore monitored interest rates in financial markets and adopted a pragmatic strategy based upon the following principles to manage interest rate risks:

- if it had been felt that there was a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.

- if it had been felt that there was a significant risk of a much sharper RISE in long and short term rates than initially expected, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would have been re-appraised

22. Interest rate forecasts expected only gradual rises in medium and longer-term fixed borrowing rates during 2021/22 and the two subsequent financial years until the turn of the year, when inflation concerns increased significantly. Internal, variable, or short-term rates, were expected to be the cheaper form of borrowing until well in to the second half of 2021/22.

Investment Performance

23. The main focus for treasury management in 2021/22 has continued to be ensuring the security of investments whilst generating a positive rate of return in an environment of extremely low rates. Due to the difference between the cost of borrowing and investment interest, cash balances have continued to be used to temporarily fund the capital programme. This has resulted in continued savings on the cost of borrowing and lower credit risk as the investment portfolio is reduced.

24. A continued use has been made of a range of investment instruments in order to maintain flexibility, spread risk, maximise liquidity and obtain positive interest rates. The use of money market funds and notice reserve accounts, with high rated banks, has maintained the security of funds and positive rate of return on investments.

25. A summary of the year's activity is shown at Appendix 2. The total interest earned in the year was £0.074m (2020/21 £0.143m) with an average interest rate of 0.34% (2020/21 0.37%). The investment interest earned was an increase of £0.034m against the original budget of £0.040m. The Bank Rate remained at the historically low level of 0.01% during most of 2021/22, only increasing to 0.25% in December, to 0.50% in February and again in March to 0.75%.

26. In previous years the accepted benchmark used was the 7-day London Interbank Bid rate (LIBID). From December 2021 all LIBOR settings ended and after which representative LIBOR rates were also no longer available. **SONIA (**the Sterling Overnight Index Average) rate has generally been seen as a replacement set of indices for LIBID for those benchmarking their investments. Following discussions with our Treasury advisors, Link Group, the use of the backward compounded 30-day SONIA rate was recommended as a replacement index for benchmarking.

27. The overall return on investments of 0.15% was achieved in 2021/22. This exceeded the backward compounded 30-day SONIA rate of 0.13%. By actively managing our temporary investments, seeking the best rates, and utilising spare capacity in certain accounts we have maximised the interest earned whilst operating within the constraints of the approved

Treasury Management Policy. During 2021/22 the investment income earned was £0.034m higher than budgeted due primarily to:

- Increased cash and reserve balances for 2021/22 allowed the placing of more funds on longer terms basis which has helped to achieve higher rates.
- Whilst the budget assumed Bank Rate would remain flat at 0.10%, the Bank of England increased Bank Rate to 0.25% in December 2021 with further increases to 0.50% in February 2022 and 0.75% in March 2022.

Borrowing Performance

28. The total borrowing at 31 March 2022 was £86.969m, which was within the operational borrowing limit of £155.000m. This is a net decrease of £6.500m from the opening balance of £93.469m, represented by repayments of £6.500m. All new borrowing was short term with no new long-term PWLB borrowing required in 2021/22. The table below sets out short-term borrowing taken during the year:

Date	Term	Amount	Interest Rate	Sources
05/05/2021	1 days	£11.000m	0.10%	Market Loans
05/05/2021	1 days	£5.000m	0.20%	Market Loans
	Total	£16.000m		

29. The use of reserves and cash balances to limit the requirement for new borrowing (internal borrowing) has continued to deliver savings in 2021/22, reducing investment balances rather than increasing external borrowing, in order to minimise interest costs.

30. The average borrowing interest rate during 2021/22 was 3.20% compared to 3.15% in 2020/21. This slight increase is due to the impact of fewer short term loan requirements during 2021/22 which means the weighted average rate is more aligned with the higher long term fixed rate PWLB loans already in place.

31. Of the total borrowing of £86.969m at 31 March 2021, £81.969m was with the Public Works Loans Board (PWLB) and the remaining £5.000m was a long-term market loan with Barclays.

32. The overall revenue cost of borrowing in 2021/22 was £2.811m. This was £0.129m less than the original budget estimate, reflecting increased reserve balances available for internal borrowing and a lower borrowing requirement for capital financing.

Debt Restructuring and Repayment

33. Due to the differential between current and historic interest rates it was anticipated that there would be little scope to restructure PWLB debt. This situation was monitored throughout the year and the cost of early repayment continues to outweigh any savings, therefore there was no early redemption or restructuring of debt.

Summary of Treasury Management performance for the year 2021/22

34. Investment income was £0.034m higher than budgeted reflecting additional cash and reserve balances available for investment and the accelerated increase in Bank Rate over the year.

35. Borrowing costs were £0.129m less than the original budget estimate, reflecting increased reserve balances available for internal borrowing and a lower borrowing requirement for capital financing.

36. The PCC has continued to take advantage of low-cost temporary borrowing rates where required to manage cash flow, and to maximise the use of internal borrowing available through reserve balances and capital receipts.

37. Overall Treasury Management performance against budget for 2021/22 generated a saving of £0.163m as summarised in the following table:

	2021/22 Budget £m	**2021/22 Actual £m**	**2021/22 Saving £m**
Borrowing Interest	2.940	2.811	(0.129)
Investment Interest	(0.040)	(0.074)	(0.034)
Net Position	**2.900**	**2.737**	**(0.163)**

Prudential Indicators 2021/22

Authorised Limit* for External Debt		
	2021/22 Reported Indicator £m	2021/22 Maximum YTD £m
Borrowing	175.000	102.969
Other Long Term Liabilities	0.000	0.000
Total	**175.000**	**102.969**

Operational Boundary** for External Debt		
	2021/22 Reported Indicator £m	2021/22 Maximum YTD £m
Borrowing	155.000	102.969
Other Long Term Liabilities	0.000	0.000
Total	**155.000**	**102.969**

Upper Limit on amounts invested beyond 364 days			
	2021/22 Reported Indicator £m	2021/22 Outturn £m	2021/22 Maximum YTD £m
Investments	**15.000**	**0**	**0**

***The authorised limit -** the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the PCC does not have the power to borrow above this level. The table below demonstrates that during 2021/22 the PCC has maintained gross borrowing within its authorised limit.

****The operational boundary** – the operational boundary is the expected borrowing position of the PCC during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

7 Investment Activity

Investments maturing during the year		
	2020/21	**2021/22**
Number of investments made in the previous year, maturing in the reporting year	1	2
Number of investments made in the reporting year, maturing in the reporting year	702	754
Total number of investments maturing in the reporting year	701	756
Number of investments made in reporting year, maturing in the following year	2	3

Average duration of investments		
	2020/21	**2021/22**
Average duration of investments (including overnight)	2 days	2 days
Average duration of investments (excluding overnight)	68 days	48 days

Summary of non-specified investments		
	2020/21	**2021/22**
Non-specified investments: Rated non-high Approved limit Maximum level invested	 75% 18%	 75% 41%
Not Rated Approved limit Maximum level invested*	 0% 3.1%	 0% 0%
Investments over 364 days Approved limit Maximum level invested	 20% 0%	 20% 0%

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9 *The *Not Rated* investment in 2020/21 related to a small impaired balance remaining with Heritable Bank. The balance did not change up to its final redemption in September 2020; however, the value relative to total investments could vary on a particular day.

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Gross Debt and Capital Financing Requirement (CFR)

Gross Debt and CFR	2021/22 Estimate £m	2021/22 Outturn £m
Borrowing as at 31 March	86.969	86.969
Capital Financing Requirement as at 31 March	122.178	112.084
Amount of Borrowing (over) / under CFR	**35.209**	**25.115**

- Total borrowing at 31 March 2022 was lower than the Capital Financing Requirement (CFR) by £25.115m.
- Borrowing at 31 March 2022 was in line with the original estimate.
- The actual CFR at 31 March 2022 was lower than the original estimate as a result of the underspend against the capital programme for 2020/21 and 2021/22.