Agenda Item	9b.
Report No	RES/28/21

HIGHLAND COUNCIL

Committee:	**Corporate Resources Committee**
Date:	25 August 2021
Report Title:	**Annual Treasury Management Report – 2020/21**
Report By:	Executive Chief Officer- Resources and Finance

1. Purpose/Executive Summary

1.1 This report on treasury management for the financial year 2020/21 is prepared in compliance with the Chartered Institute of Public Finance and Accountancy's (CIPFA) revised Code of Practice on Treasury Management in Local Authorities.

1.2 The report highlights the Council's treasury management activities undertaken, provides a commentary on the year and compares activity to the expected activities contained in the annual Treasury Strategy Statement and Investment Statement which was approved by The Highland council on 12 March 2020.

1.3 The Prudential Code also requires the Council to report the actual prudential indicators after the financial year end and these are shown in **Appendix 1.**

2. Recommendations

2.1 Members are asked to:

i. Consider the Annual Treasury Management report for 2020/21.

3. Implications

3.1 Resource implications include the cost of borrowing to fund the capital programme and are covered in section 7 and Risk implications are covered in section 8.

3.2 There are no Legal, Community (Equality, Poverty and Rural), Climate Change/Carbon Clever or Gaelic implications arising as a direct result of this report.

4. Background

4.1 The Local Government in Scotland Act 2003 (the Act) and supporting regulations requires the Council to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice. The CIPFA Code of Practice on Treasury Management (November 2009) was adopted by the Council on 4 March 2010. The Code was further updated in December 2017 with changes applying to financial year 2020/21 onwards. The Council fully complies with the Code requirements.

4.2 The primary requirements of the Code are the:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the Council of an Annual Strategy Report for the year ahead, a mid–year report and an Annual Review Report of the previous year.
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
- Delegation by the Council of the role of scrutiny of treasury management policies to a specific named body, which in this Council is the Corporate Resources Committee.

4.3 Treasury Management is defined as: "*The management of the local authority's 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*".

4.4 This report sets out:

- An overview of the strategy agreed for 2020/21 considering the economy and interest rates position for the year and incorporating the professional views of the Council's external treasury management advisors (section 5).
- Performance measurement for the year including the Council's treasury position at 31 March 2021 compared to the previous financial year (section 6)
- A summary of treasury decisions taken and effects on the revenue budget (section 7)
- A commentary on performance and risk (section 8)
- A review of compliance with the Council's procedures and Prudential Indicators (sections 9 and 10)

5. The strategy agreed for 2020/21

5.1 The expectation for interest rates within the strategy for 2020/21 was that investment yields were likely to remain low during 2020/21 but to be on a gently rising trend over the next few years and beyond with gradually increasing Public Works Loan Board (PWLB) rates forecast. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period.

5.2 The treasury strategy was to continue to use short term borrowing to fund the capital programme but to consider a strategy of de-risking by taking longer term borrowing PWLB borrowing with the aim of mitigating the risk of increased borrowing cost as interest rates start to rise.

5.3 The narrative in sections 5.3 to 5.8 of this report reflects information provided by Link Asset Services, the Council's treasury advisor.

PWLB rates are based on gilt (UK Government bonds) yields through HM Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation and the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years. We have seen, over the last two years, many bond yields up to 10 years in the Eurozone turn negative on expectations that the EU would struggle to get growth rates and inflation up from low levels. In addition, there has, at times, been an inversion of bond yields in the US whereby 10-year yields have fallen below shorter-term yields. In the past, this has been a precursor of a recession.

5.4 Gilt yields fell sharply from the start of 2020 and then spiked up during a financial markets melt down in March caused by the pandemic hitting western countries; this was rapidly countered by central banks flooding the markets with liquidity. While US treasury yields do exert influence on UK gilt yields so that the two often move in tandem, they have diverged during the first three quarters of 2020/21 but then converged in the final quarter. Expectations of economic recovery started earlier in the US than the UK but once the UK vaccination programme started making rapid progress in the new year of 2021, gilt yields and gilt yields and PWLB rates started rising sharply as confidence in economic recovery rebounded. Financial markets also expected Bank Rate to rise quicker than in the forecast tables in this report.

At the close of the day on 31 March 2021, all gilt yields from 1 to 5 years were between 0.19 – 0.58% while the 10-year and 25-year yields were at 1.11% and 1.59%.

5.5 HM Treasury imposed two changes of margins over gilt yields for PWLB rates in 2019/20 without any prior warning. The first took place on 9th October 2019, adding an additional 1% margin over gilts to all PWLB period rates. That increase was then, at least partially, reversed for some forms of borrowing on 11th March 2020, but not for mainstream non-HRA capital schemes. A consultation was then held with local authorities and on 25th November 2020, the Chancellor announced the conclusion to the review of margins over gilt yields for PWLB rates; the standard and certainty margins were reduced by 1% but a prohibition was introduced to deny access to borrowing from the PWLB for any local authority which had purchase of assets for yield in its three year capital programme. The new margins over gilt yields are as follows: -.

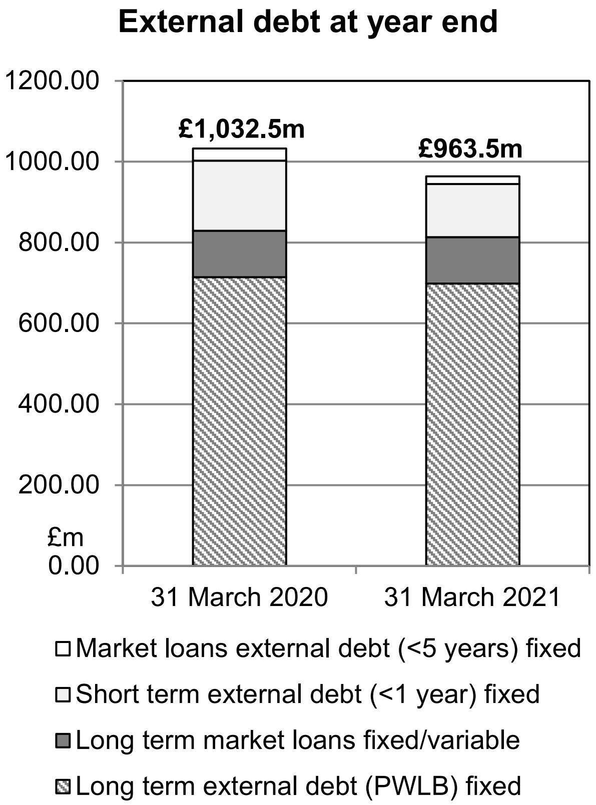
- PWLB Standard Rate is gilt plus 100 basis points (G+100bps)
- PWLB Certainty Rate is gilt plus 80 basis points (G+80bps)
- PWLB HRA Standard Rate is gilt plus 100 basis points (G+100bps)
- PWLB HRA Certainty Rate is gilt plus 80bps (G+80bps)
- Local Infrastructure Rate is gilt plus 60bps (G+60bps)

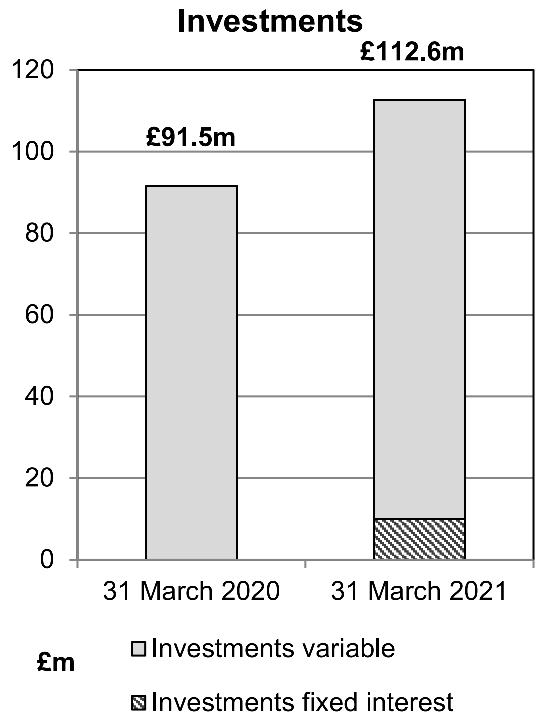
5.6 There is likely to be only a gentle rise in gilt yields and PWLB rates over the next three years as Bank Rate is not forecast to rise from 0.10% by March 2024 as the Bank of England has clearly stated that it will not raise rates until inflation is sustainably above its target of 2%; this sets a high bar for Bank Rate to start rising.

5.7 Further information on the economy and interest rates during the year can be found at **Appendix 2**.

6. Performance measurement

6.1 The treasury position at the 31 March 2021 compared with the previous year is shown in the graphs below.





Average interest rates comparison	31/03/20	31/03/21
Short term external debt (<1 year) fixed	0.92%	0.29%
Market loans fixed/variable	4.04%	4.24%
Long term external debt (PWLB) fixed	4.26%	4.18%
Total debt	**3.67%**	**3.66%**
Investments fixed interest	-	0.00%
Investments variable	0.36%	0.01%
Total investments	**0.36%**	**0.01%**

6.2 The figures show a marginal decrease in the average interest rate on external debt borrowings from 3.67% at March 2019 to 3.66% at March 2021. The investment return for 2020/21 was lower than the previous year following the bank rate decrease to 0.10% on 19 March.

6.3 Details of all PWLB long term borrowing repaid, is in **Appendix 3** and all external borrowing is in **Appendix 4.** The average rate for temporary loans at 31 March 2021 was 0.29%.

7. Treasury decisions taken and revenue effects

Borrowing requirement and debt

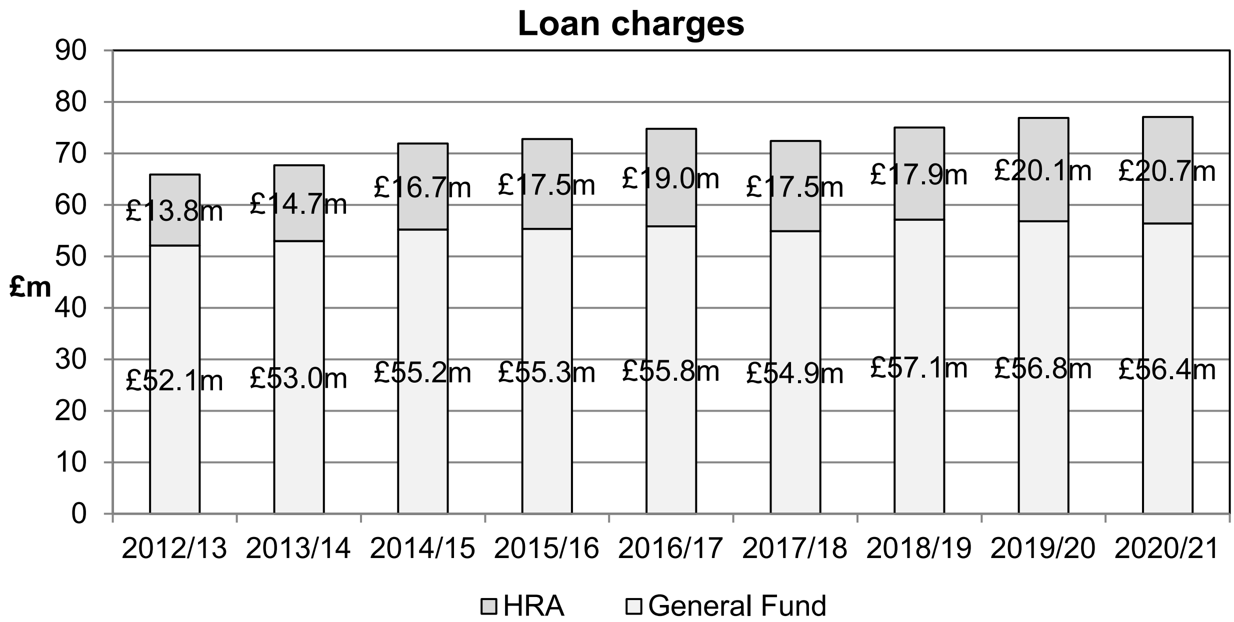
7.1 The Council undertakes capital expenditure on long-term assets which is funded as follows:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing requirement.

7.2 The total net capital expenditure for 2020/21 was £43.0m (General Fund £18.8m and HRA £24.2m) against planned net capital expenditure of £58.0m (General Fund £31.1m and HRA £26.9m). Reasons for variations in Service and project capital expenditure for the year are reported to Strategic Committees as part of the final 2020/21 out-turn capital monitoring process. Details of gross and net capital spend for the year and the borrowing requirement against the estimated position are in **Appendix 1**.

7.3 There has been a reduction in external debt of £69.0m (see graph at **para 6.1**) which is more than the borrowing requirement of £3.5m. The Council is currently under-borrowed by £67.9m (6.58% of the underlying borrowing requirement of £1,031.4m). This means that the underlying borrowing requirement is also funded by internal borrowing as well as the external borrowing noted above (explained in more detail at **para 10.5**).

7.4 In terms of the impact on revenue budgets, the increased capital expenditure has increased the level of loan charges the Council has incurred. The graph below shows the changes in loans charges over the last 9 years.



7.5 Due to the level of capital expenditure, financing costs (loan charges) are a significant proportion of the Council's net revenue stream. The ratio of financing costs to net revenue stream for the general fund including PPP/NPD is 11.4% (estimate 13.2%) and 37.7% for HRA (estimate 38.0%) (**Appendix 1, prudential indicator 4**). The reason for the general fund ratio being lower than estimated is due to the significant increase in the overall Council budget during 2020/21 from additional COVID-19 response funding received from Government.

7.6 Rescheduling

There was no rescheduling completed during 2020/21. While refinancing rates were closely monitored throughout the year no significant opportunities arose to make savings due to breakage costs.

7.7 A summary of outstanding deferred revenue costs attributable to debt rescheduling exercises undertaken in years to date, is provided in the table below. These represent early debt repayment costs (premiums) and discounts, associated with debt rescheduling. It is accounting practice for these to be written off over the periods of the new loans taken as part of the rescheduling and included as part of the annual loan charges.

	Outstanding 31 Mar 2020	**Incurred 2020/21**	**Written off 2020/21**	**Outstanding 31 Mar 2021**
	£000	**£000**	**£000**	**£000**
Premiums	25,551	-	(1,992)	23,559
Discounts	(6,801)	-	39	(6,762)
Net Deferred Revenue Costs	18,750	-	(1,952)	16,797

7.8 Overall performance

The Council's average borrowing and investment rate for the year was 3.70% compared to 3.85% in 2019/20. As stated above (**para 6.2**), all capital expenditure was funded using short term borrowing at lower rates than forecast and replacing PWLB maturities with lower rate borrowing.

7.9 Revenue effect: The final position shows an underspend for the General Fund loans charges (£0.206m) and an underspend for HRA (£0.242) compared to budget for the year. The underspend was due to low interest rates for short term borrowing and lower levels of capital expenditure than planned due to COVID-19 restrictions impacting the progress of capital projects.

7.10 Investments held by the Council

The Council's investment policy is governed by the Scottish Government Investment Regulations, which were adopted in the Annual Investment Strategy 2010/11 and approved by the Council on 24 June 2010. This policy sets out the approach for choosing investment categories and counterparties and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

7.11 The Council's policy states the maximum investment period is 2 years. However, during 2020/21 deposits were placed for periods of 1 year or less than 1 year to reflect credit risk.

7.12 The Council maintained an average end of month balance of £97.1m of internally managed funds which earned an average rate of return of 0.15%. The comparable performance indicator is the average 7-day LIBID rate, which was -0.07% for 2020/21. No institutions in which investments were made showed any difficulty in repaying the investment and interest in full during the year.

8. Performance and risk

8.1 In the current debt portfolio at 31 March 2021, 73% (£698.7m) of the total gross debt is at fixed long-term rates with the PWLB.

8.2 All major borrowing and capital financing requirement (CFR) decisions taken by officers were discussed with the Council's external treasury management advisors.

8.3 Returns on the Council's investments are predominantly determined by short-term variable rates. Whilst this can introduce an element of volatility to returns, it is minimal in terms of the total debt portfolio. Risk, in relation to the potential loss of principal, is minimised through the Council's restricted lending list (using a diversified list of counter-parties and based on credit assessment).

8.4 The Council uses several money market brokers to facilitate short-term borrowing and investment deals. This ensures competitive market rates are obtained. All brokers charged the same level of commission per transaction and performed satisfactorily. In addition, the Council's treasury management officers have direct lines to some major banks to facilitate direct investment with suitably rated institutions.

8.5 Short term borrowing decreased from £173.5m (31/03/20) to £131.0m (31/03/21) and levels of short-term borrowing are likely to remain high. However, in order to mitigate exposure to interest rate risk, PWLB rates will be monitored and longer term borrowing undertaken where rates are favourable.

9. Compliance with the Council's procedures and Prudential Indicators

9.1 The Council complied with its internal procedures and the requirements of the CIPFA Code of Practice on Treasury Management. The Council is bound by best practice requirements, which involve limits to be set and adhered to in relation to short-term borrowing and exposure to variable interest rates and complied with these throughout the year (**Appendix 1, indicator 10**).

10. The Prudential Code – Indicators

10.1 The Council is required by the Prudential Code to report the actual treasury position compared to the prudential indicators at the year-end. **Appendix 1** provides details of all the mandatory, estimated and actual prudential indicators for the year 2020/21.

10.2 <u>Capital Financing Requirement (CFR)</u>

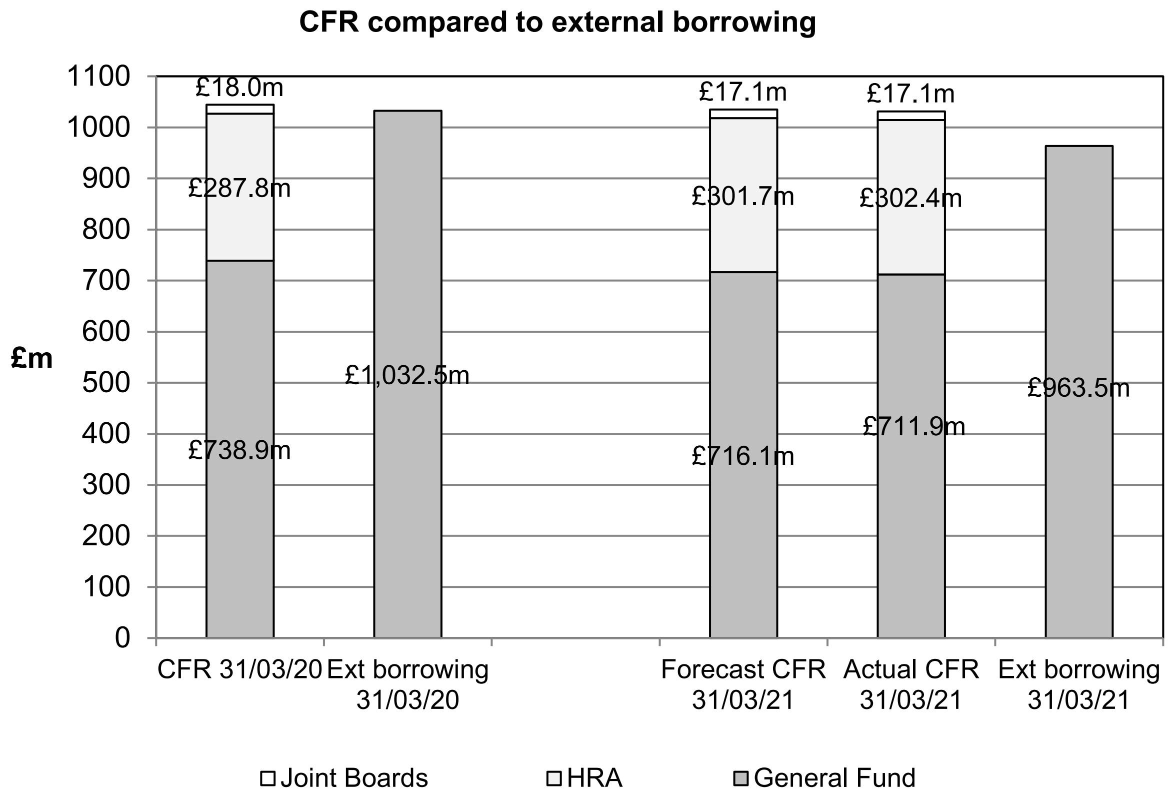
The CFR represents the accumulated net capital expenditure which the Council requires to fund by way of long term borrowing and other capital financing, until the capital projects, comprising the CFR, are fully written off to revenue (mainly by way of annual loan charges).

10.3 In recent years the Council has been in a position whereby its CFR is greater than its long-term borrowing. This results from the Council using internal cash sources, as well as long-term borrowing to finance the CFR. The use of internal cash sources can represent a more effective and low-cost option for financing, compared to long-term borrowing, given the low returns available on short-term deposits when compared to PWLB rates, even in the current low borrowing rate environment.

10.4 However, the Council must keep the CFR and long-term borrowing position under regular review, as the use of internal cash sources can result in increased re-financing risk i.e. if internal cash sources are utilised, and the Council has no choice but to borrow, and not necessarily at a time of its choosing, borrowing costs could be impacted.

10.5 The CFR is kept under regular review, and in recent years part of the annual treasury strategy has been to take steps to manage the CFR versus long-term borrowing position to an acceptable level. As shown in the graph below the difference between CFR and external borrowing stood at £67.9m as at 31 March 2021. This position will be kept under regular review as part of the Council's on-going treasury management.

10.6 In order to ensure that over the medium-term borrowing net of investments will only be for a capital purpose, net borrowing should not, except in the short term, exceed the CFR for 2020/21. The graph below shows that the Council has complied with this requirement.



10.7 Borrowing Limits

The Council is required to agree an Authorised Limit for borrowing for the year. This figure provides for estimated contingencies which may require to be funded in the year in addition to planned capital expenditure.

10.8 The Operational Boundary, also approved by the Council in compliance with the Code, is the expected borrowing position of the Council 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.

10.9 During 2020/21 the Council complied with both the Authorised Limit and Operational Boundaries and the maximum is reported at **Appendix 1 indicator 5 and 6.**

Designation: Head of Corporate Finance and Commercialism

Date: 10 August 2021

Author: Catriona Stachan, Accountant

Background Papers: Treasury system and financial ledger reports
Treasury Strategy Statement and Investment Strategy 2020/21

Appendix 1

Estimated and Actual Treasury Position and Prudential Indicators

		2020/21 Indicator £m	2020/21 Actual £m
1	**Capital expenditure**		
	Gross capital expenditure		
	General Fund including PPP/NPD	96.0	76.6
	Housing Revenue Account	41.9	48.8
	Total gross capital expenditure	**137.9**	**125.4**
	Income		
	General Fund	(64.9)	(57.8)
	HRA	(15.0)	(24.6)
	Total income	**(79.9)**	**(82.4)**
	Net capital expenditure		
	General Fund	31.1	18.8
	HRA	26.9	24.2
	Total net capital expenditure	**58.0**	**43.0**
	Loan charge instalments		
	General Fund	(30.8)	(29.9)
	HRA	(10.1)	(9.6)
	Total instalments	**(40.9)**	**(39.5)**
	Net borrowing for new capital expenditure		
	General Fund	0.3	(11.1)
	HRA	16.8	14.6
	Total net borrowing for new capital expenditure	**17.1**	**3.5**
2	**Capital Financing Requirement (CFR) at 31 March**		
	General Fund excluding PPP/NPD	716.1	711.9
	Housing Revenue Account	301.7	302.4
	PPP/NPD	142.1	143.4
	Sub-total (as per HC annual accounts)	**1,159.9**	**1,157.7**
	Joint Boards	17.1	17.1
	Total	**1,177.0**	**1,174.8**
	Sub-total excluding PPP/NPD	**1,034.9**	**1,031.4**

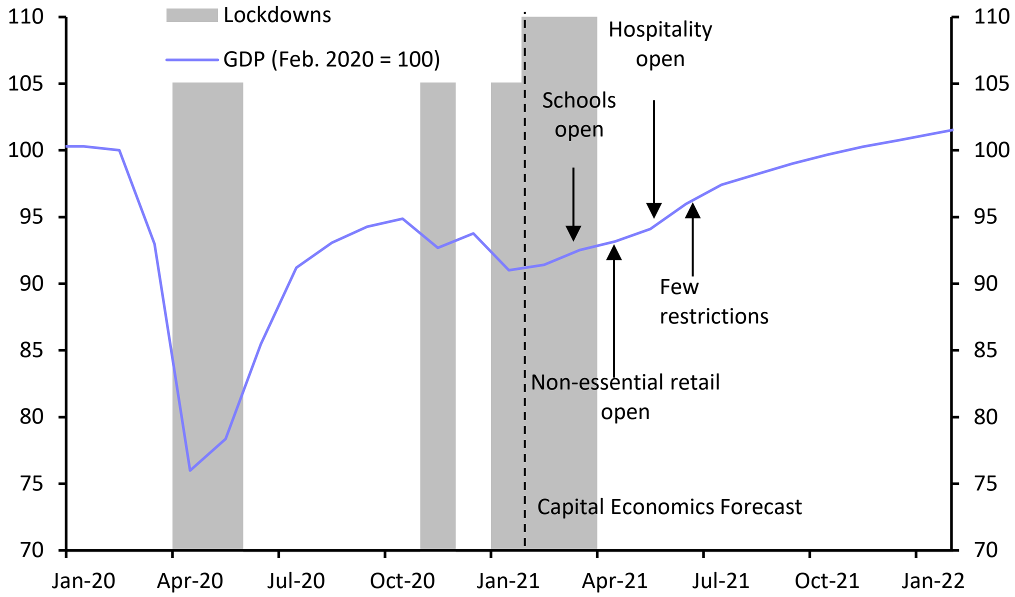
		2020/21 Indicator £m	2020/21 Actual £m
3	**Treasury Position at 31 March**		
	Borrowing – Long term	799.3	832.5
	Borrowing – Short term	209.6	131.0
	Other Long-Term Liabilities (PPP)	142.1	143.4
	Total Debt	**1,151.0**	**1,106.9**
	Investments	50.0	112.6
	Net Borrowing	**1,101.0**	**994.3**
4	**Ratio of financing costs to net revenue stream**		
	General Fund including PPP	13.2%	11.4%
	Housing Revenue Account	38.0%	37.7%
		Limit	**Maximum**
5	**Authorised Limit for Borrowing**	1,063.1	1,032.5 April 20
6	**Operational Boundary for Borrowing**	1,037.0	1,032.5 April 20
7	**Interest rate exposures of debt net of investments**		
	Upper Limit (Fixed)	1,034.8	917.0 March 2021
	Upper Limit (Variable)	362.2	21.2 Dec 2020
8	**Maturity structure of fixed rate borrowing**		
	Under 12 months	30.0%	17.0% June 2020
	12 months to 2 years	30.0%	3.6% Sept & Dec 2020
	2 years to 5 years	40.0%	4.5% June 2020
	5 years to 10 years	50.0%	12.8% Sept & Dec 2020
	10 years and above	100.0%	66.0% Sept & Dec 2020
9	**Upper limit for the maturing of investments made for periods longer than 364 days (against maximum position**)	£20.0m	Nil
10	**Short term borrowing (net of investments) as a % of outstanding long-term debt (maximum position)**	25.0%	16.6% April 2020
	Variable interest debt (net of investments) as a % of outstanding long-term debt (maximum position)	35.0%	3.9% Sept & Dec 2020

Appendix 2

Economic update provided by the Council's Treasury Advisor (Link Asset Services)

UK. Coronavirus. The financial year 2020/21 will go down in history as being the year of the pandemic. The first national lockdown in late March 2020 did huge damage to an economy that was unprepared for such an eventuality. This caused an economic downturn that exceeded the one caused by the financial crisis of 2008/09. A short second lockdown in November did relatively little damage but by the time of the third lockdown in January 2021, businesses and individuals had become more resilient in adapting to working in new ways during a three month lockdown so much less damage than was caused than in the first one.

The advent of vaccines starting in November 2020, were a game changer. The way in which the UK and US have led the world in implementing a fast programme of vaccination which promises to lead to a return to something approaching normal life during the second half of 2021, has been instrumental in speeding economic recovery and the reopening of the economy. In addition, the household saving rate has been exceptionally high since the first lockdown in March 2020 and so there is plenty of pent-up demand and purchasing power stored up for services in the still-depressed sectors like restaurants, travel and hotels as soon as they reopen. It is therefore expected that the UK economy could recover its pre-pandemic level of economic activity during quarter 1 of 2022.



Both the Government and the Bank of England took rapid action in March 2020 at the height of the crisis to provide support to financial markets to ensure their proper functioning, and to support the economy and to protect jobs.

The Monetary Policy Committee cut Bank Rate from 0.75% to 0.25% and then to 0.10% in March 2020 and embarked on a £200bn programme of quantitative easing QE (purchase of gilts so as to reduce borrowing costs throughout the economy by lowering gilt yields). The MPC increased then QE by £100bn in June and by £150bn in November to a total of £895bn. While Bank Rate remained unchanged for the rest of the year, financial markets were concerned that the MPC could cut Bank Rate to a negative rate; this was firmly discounted at the February 2021 MPC meeting when it was established that commercial banks would be unable to implement negative rates for at least six months – by which time the economy was expected to be making a strong recovery and negative rates would no longer be needed.

Average inflation targeting. This was the major change adopted by the Bank of England in terms of implementing its inflation target of 2%. The key addition to the Bank's forward guidance in August was a new phrase in the policy statement, namely that "it does not intend to tighten monetary policy until there is clear evidence that significant progress is being made in eliminating spare capacity and achieving the 2% target sustainably". That seems designed to say, in effect, that even if inflation rises to 2% in a couple of years' time, do not expect any action from the MPC to raise Bank Rate – until they can clearly see that level of inflation is going to be persistently above target if it takes no action to raise Bank Rate. This sets a high bar for raising Bank Rate and no increase is expected by March 2024, and possibly for as long as five years. Inflation has been well under 2% during 2020/21; it is expected to briefly peak at just over 2% towards the end of 2021, but this is a temporary short-lived factor and so not a concern to the MPC.

Government support. The Chancellor has implemented repeated rounds of support to businesses by way of cheap loans and other measures and has protected jobs by paying for workers to be placed on furlough. This support has come at a huge cost in terms of the Government's budget deficit ballooning in 20/21 and 21/22 so that the Debt to GDP ratio reaches around 100%. The Budget on 3rd March 2021 increased fiscal support to the economy and employment during 2021 and 2022 followed by substantial tax rises in the following three years to help to pay the cost for the pandemic. This will help further to strengthen the economic recovery from the pandemic and to return the government's finances to a balanced budget on a current expenditure and income basis in 2025/26. This will stop the Debt to GDP ratio rising further from 100%. An area of concern, though, is that the government's debt is now twice as sensitive to interest rate rises as before the pandemic due to QE operations substituting fixed long-term debt for floating rate debt; there is, therefore, much incentive for the Government to promote Bank Rate staying low e.g. by using fiscal policy in conjunction with the monetary policy action by the Bank of England to keep inflation from rising too high, and / or by amending the Bank's policy mandate to allow for a higher target for inflation.

BREXIT. The final agreement on 24th December 2020 eliminated a significant downside risk for the UK economy. The initial agreement only covered trade so there is further work to be done on the services sector where temporary equivalence has been granted in both directions between the UK and EU; that now needs to be formalised on a permanent basis. There was much disruption to trade in January as form filling has proved to be a formidable barrier to trade. This appears to have eased somewhat since then but is an area that needs further work to ease difficulties, which are still acute in some areas.

USA. The US economy did not suffer as much damage as the UK economy due to the pandemic. The Democrats won the presidential election in November 2020 and have control of both Congress and the Senate, although power is more limited in the latter. This enabled the Democrats to pass a $1.9trn (8.8% of GDP) stimulus package in March on top of the $900bn fiscal stimulus deal passed by Congress in late December. These, together with the vaccine rollout proceeding swiftly to hit the target of giving a first jab to over half of the population within the President's first 100 days, will promote a rapid easing of restrictions and strong economic recovery during 2021. The Democrats are also planning to pass a $2trn fiscal stimulus package aimed at renewing infrastructure over the next decade. Although this package is longer-term, if passed, it would also help economic recovery in the near-term.

After Chair Jerome Powell spoke on the Fed's adoption of a flexible average inflation target in his Jackson Hole speech in late August 2020, the mid-September meeting of the Fed agreed a new inflation target - that "it would likely be appropriate to maintain the current target range until labour market conditions were judged to be consistent with the Committee's assessments of maximum employment and inflation had risen to 2% and was on track to moderately exceed 2% for some time." This change was aimed to provide more stimulus for economic growth and higher levels of employment and to avoid the danger of getting caught in a deflationary "trap" like Japan. It is to be noted that inflation has actually been under-shooting the 2% target significantly for most of the last decade, (and this year), so financial markets took note that higher levels of inflation are likely to be in the pipeline; long-term bond yields duly rose after the meeting. There is now some expectation that where the Fed has led in changing its policy towards implementing its inflation and full employment mandate, other major central banks will follow, as indeed the Bank of England has done so already. The Fed expects strong economic growth during 2021 to have only a transitory impact on inflation, which explains why the majority of Fed officials project US interest rates to remain near-zero through to the end of 2023. The key message is still that policy will remain unusually accommodative – with near-zero rates and asset purchases – continuing for several more years. This is likely to result in keeping treasury yields at historically low levels. However, financial markets in 2021 have been concerned that the sheer amount of fiscal stimulus, on top of highly accommodative monetary policy, could be over-kill leading to a rapid elimination of spare capacity in the economy and generating higher inflation much quicker than the Fed expects. They have also been concerned as to how and when the Fed will eventually wind down its programme of monthly QE purchases of treasuries. These concerns have pushed treasury yields sharply up in the US in 2021 and is likely to have also exerted some upward pressure on gilt yields in the UK.

EU. Both the roll out and take up of vaccines has been disappointingly slow in the EU in 2021, at a time when many countries are experiencing a sharp rise in cases which are threatening to overwhelm hospitals in some major countries; this has led to renewed severe restrictions or lockdowns during March. This will inevitably put back economic recovery after the economy had staged a rapid rebound from the first lockdowns in Q3 of 2020 but contracted slightly in Q4 to end 2020 only 4.9% below its pre-pandemic level. Recovery will now be delayed until Q3 of 2021 and a return to pre-pandemic levels is expected in the second half of 2022.

Inflation was well under 2% during 2020/21. The ECB did not cut its main rate of -0.5% further into negative territory during 2020/21. It embarked on a major expansion of its QE operations (PEPP) in March 2020 and added further to that in its December 2020 meeting when it also greatly expanded its programme of providing cheap loans to banks. The total PEPP scheme of €1,850bn is providing protection to the sovereign bond yields of weaker countries like Italy. There is, therefore, unlikely to be a euro crisis while the ECB is able to maintain this level of support.

China. After a concerted effort to get on top of the virus outbreak in Q1 of 2020, economic recovery was strong in the rest of the year; this has enabled China to recover all of the contraction in Q1. Policy makers have both quashed the virus and implemented a programme of monetary and fiscal support that has been particularly effective at stimulating short-term growth.

Japan. Three rounds of government fiscal support in 2020 together with Japan's relative success in containing the virus without draconian measures so far, and the roll out of vaccines gathering momentum in 2021, should help to ensure a strong recovery in 2021 and to get back to pre-virus levels by Q3.

World growth. World growth was in recession in 2020. Inflation is unlikely to be a problem in most countries for some years due to the creation of excess production capacity and depressed demand caused by the coronavirus crisis.

Deglobalisation. Until recent years, world growth has been boosted by increasing globalisation i.e. countries specialising in producing goods and commodities in which they have an economic advantage and which they then trade with the rest of the world. This has boosted worldwide productivity and growth, and, by lowering costs, has also depressed inflation. However, the rise of China as an economic superpower over the last 30 years, which now accounts for nearly 20% of total world GDP, has unbalanced the world economy. In March 2021, western democracies implemented limited sanctions against a few officials in charge of government policy on the Uighurs in Xinjiang; this led to a much bigger retaliation by China and is likely to mean that the China / EU investment deal then being negotiated, will be torn up. After the pandemic exposed how frail extended supply lines were around the world, both factors are now likely to lead to a sharp retrenchment of economies into two blocs of western democracies v. autocracies. It is, therefore, likely that we are heading into a period where there will be a reversal of world globalisation and a decoupling of western countries from dependence on China to supply products and vice versa. This is likely to reduce world growth rates.

Central banks' monetary policy. During the pandemic, the governments of western countries have provided massive fiscal support to their economies which has resulted in a big increase in total government debt in each country. It is therefore very important that bond yields stay low while debt to GDP ratios slowly subside under the impact of economic growth. This provides governments with a good reason to amend the mandates given to central banks to allow higher average levels of inflation than we have generally seen over the last couple of decades. Both the Fed and Bank of England have already changed their policy towards implementing their existing mandates on inflation, (and full employment), to hitting an average level of inflation. Greater emphasis could also be placed on hitting subsidiary targets e.g. full employment before raising rates. Higher average rates of inflation would also help to erode the real value of government debt more quickly.

Appendix 3 – PWLB Borrowing undertaken and borrowing repaid 2020/21

PWLB Borrowing undertaken during 2020/21

None

PWLB Borrowing repaid during 2020/21

Month repaid	**Amount**	**Purpose of borrowing**	**Duration**	**Rate**
Sept 2020	£9.83m	Capital programme	25 years	8.250%
March 2021	£0.40m	Capital programme	32 years	9.375%
March 2021	£3.00m	Capital programme	35 years	9.125%
Sept 2020	£0.87m	NHT	6.3 years	3.150%
March 2021	£0.43m	NHT	6.2 years	3.020%
March 2021	£0.92m	NHT	6.0 years	2.890%
March 2021	£0.60m	NHT	6.1 years	2.310%
Total	**£16.06m**			

Appendix 4 – External Borrowing at 31 March 2021

Market loans fixed

Deal Ref	Start Date	Maturity Date	Counterparty	Profile	Rate	Principal O/S (£)
M290054	01/04/16	01/04/21	Waverley Borough Council	Maturity	1.50%	4,000,000.00
M290056	14/04/16	14/04/21	Guildford Borough Council	Maturity	1.50%	5,000,000.00
M290050	03/08/04	03/02/65	Barclays Bank plc	Maturity	5.05%	11,900,000.00
M290048	02/12/03	02/12/65	Barclays Bank plc	Maturity	5.00%	25,200,000.00
M290049	02/12/03	02/12/65	Barclays Bank plc	Maturity	5.00%	25,000,000.00
M290052	23/03/06	23/03/66	Barclays Bank plc	Maturity	3.80%	16,216,000.00
M290064	08/02/21	08/02/24	Cornwall Council	Maturity	1.00%	10,000,000.00
				Average rate	4.12%	97,316,000.00

Short term external debt (< 1 year) fixed

Deal Ref	Start Date	Maturity Date	Counterparty	Profile	Rate	Principal O/S (£)
T503391	08/07/20	08/04/21	Renfrewshire Council	Maturity	0.45%	5,000,000.00
T503395	15/07/20	15/04/21	West Yorkshire Combined Authority	Maturity	0.37%	5,000,000.00
T503393	17/07/20	19/04/21	West Northamptonshire Council	Maturity	0.40%	5,000,000.00
T503402	29/10/20	30/04/21	Teesside Pension Fund	Maturity	0.15%	6,000,000.00
T503403	13/11/20	13/05/21	East Renfrewshire Council	Maturity	0.20%	5,000,000.00
T503400	17/11/20	17/05/21	Edinburgh City Council	Maturity	0.15%	5,000,000.00
T503401	17/11/20	17/05/21	Lichfield District Council	Maturity	0.13%	2,000,000.00
T503389	27/05/20	26/05/21	Gloucestershire County Council	Maturity	0.85%	5,000,000.00
T503396	15/07/20	30/06/21	West Yorkshire Combined Authority	Maturity	0.42%	5,000,000.00
T503416	08/01/21	08/07/21	Renfrewshire Council	Maturity	0.10%	5,000,000.00
T503394	13/07/20	12/07/21	Devon County Council	Maturity	0.42%	5,000,000.00
T503392	20/07/20	19/07/21	Renfrewshire Council	Maturity	0.50%	5,000,000.00
T503399	09/11/20	09/08/21	Chichester District Council	Maturity	0.20%	3,000,000.00
T503412	13/11/20	13/08/21	South Lanarkshire Council	Maturity	0.18%	5,000,000.00
T503407	02/12/20	02/09/21	Orkney Islands Council	Maturity	0.18%	5,000,000.00
T503398	09/11/20	08/09/21	South Ribble Borough Council	Maturity	0.21%	5,000,000.00
T503418	29/03/21	29/09/21	Tendring District Council	Maturity	0.05%	3,000,000.00
T503404	11/11/20	11/10/21	Shropshire Council	Maturity	0.30%	5,000,000.00
T503408	30/11/20	29/10/21	North Somerset District Council	Maturity	0.25%	3,000,000.00
T503411	11/11/20	04/11/21	North Somerset District Council	Maturity	0.30%	3,000,000.00
T503397	09/11/20	08/11/21	Fylde Borough Council	Maturity	0.25%	2,000,000.00
T503410	12/11/20	11/11/21	Gloucestershire County Council	Maturity	0.30%	5,000,000.00
T503413	15/01/21	23/11/21	Shropshire Council	Maturity	0.28%	5,000,000.00
T503409	03/12/20	02/12/21	Mansfield District Council	Maturity	0.25%	2,000,000.00
T503405	09/12/20	08/12/21	Bath and North East Somerset Council	Maturity	0.34%	5,000,000.00
T503406	09/12/20	08/12/21	London Borough of Redbridge	Maturity	0.34%	5,000,000.00
T503414	07/01/21	06/01/22	Tyne And Wear Integrated Transport Authority	Maturity	0.25%	5,000,000.00
T503415	07/01/21	06/01/22	London Borough of Wandsworth	Maturity	0.25%	5,000,000.00
T503419	08/03/21	11/01/22	Darlington Borough Council	Maturity	0.13%	5,000,000.00
T503417	29/01/21	26/01/22	Castle Point Borough Council	Maturity	0.14%	2,000,000.00
				Average rate	0.29%	131,000,000.00

Long term market loans fixed/variable (Lender Option Borrower Option)

Deal Ref	Start Date	Maturity Date	Counterparty	Profile	Rate	Principal O/S (£)
M290045	30/09/02	30/09/42	Bank of Scotland plc	Maturity	4.50%	5,000,000.00
M240007	12/12/90	12/12/50	Coventry Building Society Superannuation Fund	Maturity	11.12%	1,000,000.00
M290051	26/10/04	26/10/54	Dexia Public Finance Bank	Maturity	4.34%	8,750,000.00
M290046	14/03/03	16/03/65	Dexia Public Finance Bank	Maturity	4.40%	10,000,000.00
M290047	14/03/03	16/03/65	Dexia Public Finance Bank	Maturity	4.40%	11,740,000.00
				Average rate	4.58%	36,490,000.00

Long term external debt (PWLB) fixed

Deal Ref	Start Date	Maturity Date	Counterparty	Profile	Rate	Principal O/S (£)
P472856	25/03/93	30/09/21	PWLB	Maturity	9.37%	1,000,000.00
P450549	18/10/82	30/09/22	PWLB	Maturity	10.50%	1,053,479.77
P479600	24/06/97	30/09/22	PWLB	Maturity	7.12%	13,800,000.00
P498767	14/07/11	30/09/22	PWLB	Maturity	4.35%	15,000,000.00
P505331	31/08/16	31/03/23	PWLB	Maturity	1.21%	1,200,000.00
P452310	06/06/83	31/03/23	PWLB	Maturity	10.37%	700,000.00
P469054	18/01/91	30/09/23	PWLB	Maturity	11.25%	400,000.00
P479824	07/08/97	31/03/24	PWLB	Maturity	6.87%	8,793,583.00
P479831	07/08/97	31/03/24	PWLB	Maturity	7.12%	766,648.00
P468141	01/03/90	30/09/24	PWLB	Maturity	10.87%	800,000.00
P499029	27/09/11	30/09/25	PWLB	Maturity	3.92%	20,000,000.00
P479272	01/05/97	31/03/27	PWLB	Maturity	7.75%	25,000,000.00
P479704	17/07/97	31/03/27	PWLB	Maturity	7.00%	25,000,000.00
P508923	22/03/19	30/09/28	PWLB	Maturity	1.90%	7,500,000
P509002	28/03/19	30/09/28	PWLB	Maturity	1.82%	7,500,000
P501784	11/12/12	30/09/27	PWLB	Maturity	3.19%	10,000,000.00
P480402	13/01/98	30/09/27	PWLB	Maturity	6.12%	5,000,000.00
P501996	15/03/13	31/03/30	PWLB	Maturity	3.70%	7,500,000.00
P502022	22/03/13	31/03/30	PWLB	Maturity	3.58%	7,500,000.00
P499165	23/11/11	30/09/30	PWLB	Maturity	3.93%	20,000,000.00
P478594	11/12/96	30/09/31	PWLB	Maturity	7.75%	11,135,901.00
P501895	26/02/13	25/07/32	PWLB	Maturity	3.94%	15,000,000.00
P454211	30/03/84	30/09/33	PWLB	Maturity	10.25%	700,000.00
P488282	02/12/03	30/09/33	PWLB	Maturity	5.00%	3,600,000.00
P502832	07/02/14	31/03/34	PWLB	Maturity	4.17%	10,000,000.00
P503806	10/03/15	30/09/34	PWLB	Maturity	3.30%	10,000,000.00
P464213	25/03/88	30/09/37	PWLB	Maturity	9.12%	702,319.85
P475185	16/02/95	30/09/44	PWLB	Maturity	9.00%	500,000.00
P476150	29/06/95	31/03/45	PWLB	Maturity	8.37%	1,000,000.00
P475184	16/02/95	30/09/45	PWLB	Maturity	8.620%	500,000.00
P475052	26/01/95	30/09/48	PWLB	Maturity	8.75%	500,000.00
P474807	24/10/94	30/09/51	PWLB	Maturity	8.62%	1,000,000.00
P492695	15/01/07	31/03/52	PWLB	Maturity	4.25%	13,500,000.00
P474808	24/10/94	30/09/52	PWLB	Maturity	8.62%	1,000,000.00
P492696	15/01/07	31/03/53	PWLB	Maturity	4.25%	23,300,000.00

Long term external debt (PWLB) fixed (continued)

Deal Ref	Start Date	Maturity Date	Counterparty	Profile	Rate	Principal O/S (£)
P474817	26/10/94	30/09/53	PWLB	Maturity	8.62%	1,000,000.00
P493071	08/03/07	30/09/53	PWLB	Maturity	4.25%	5,000,000.00
P492697	15/01/07	31/03/54	PWLB	Maturity	4.25%	20,000,000.00
P493070	08/03/07	31/03/54	PWLB	Maturity	4.25%	8,600,000.00
P474785	14/10/94	30/09/54	PWLB	Maturity	8.87%	1,000,000.00
P474818	26/10/94	30/09/54	PWLB	Maturity	8.62%	1,000,000.00
P493626	02/08/07	30/09/54	PWLB	Maturity	4.55%	10,000,000.00
P493835	23/08/07	30/09/54	PWLB	Maturity	4.45%	5,000,000.00
P476656	30/11/95	30/09/55	PWLB	Maturity	8.00%	1,000,000.00
P476790	21/12/95	30/09/55	PWLB	Maturity	7.87%	4,000,000.00
P476823	21/12/95	30/09/55	PWLB	Maturity	7.87%	1,000,000.00
P476824	21/12/95	30/09/55	PWLB	Maturity	7.87%	1,000,000.00
P477578	02/05/96	31/03/56	PWLB	Maturity	8.37%	10,000,000.00
P477622	08/05/96	31/03/56	PWLB	Maturity	8.37%	10,000,000.00
P477985	30/08/96	31/03/56	PWLB	Maturity	8.25%	3,000,000.00
49342	05/07/07	30/09/56	PWLB	Maturity	4.80%	60,000,000.00
P502887	05/03/14	30/09/57	PWLB	Maturity	4.20%	20,000,000.00
P498092	13/10/10	31/03/59	PWLB	Maturity	4.09%	10,000,000.00
P497853	06/09/10	31/03/60	PWLB	Maturity	4.03%	10,000,000.00
P509312	04/06/19	30/09/61	PWLB	Maturity	2.18%	5,000,000.00
P509461	04/07/19	31/03/62	PWLB	Maturity	2.10%	10,000,000.00
P503717	05/02/15	31/03/63	PWLB	Maturity	2.84%	20,000,000.00
P502921	18/03/14	30/09/63	PWLB	Maturity	4.19%	20,000,000.00
P505126	21/06/16	31/03/64	PWLB	Maturity	2.51%	25,000,000.00
P503301	12/09/14	31/03/64	PWLB	Maturity	3.95%	20,000,000.00
P509636	09/08/19	31/03/66	PWLB	Maturity	1.84%	10,000,000.00
P507215	05/04/18	30/09/67	PWLB	Maturity	2.27%	25,000,000.00
P507444	31/05/18	31/03/67	PWLB	Maturity	2.25%	10,000,000.00
P509848	05/09/19	31/03/67	PWLB	Maturity	1.58%	10,000,000.00
P509723	19/08/19	31/03/68	PWLB	Maturity	1.74%	10,000,000.00
P509506	09/07/19	30/09/68	PWLB	Maturity	2.03%	5,000,000.00
P169721	11/03/20	30/09/69	PWLB	Maturity	2.07%	5,000,000.00
P175073	24/03/20	30/09/69	PWLB	Maturity	1.48%	29,800,000.00
P509289	30/05/19	31/03/69	PWLB	Maturity	2.19%	5,000,000.00
P509372	18/06/19	31/03/69	PWLB	Maturity	2.11%	5,000,000.00
P509495	08/07/19	31/03/69	PWLB	Maturity	2.01%	5,000,000.00
P509629	08/08/19	31/03/69	PWLB	Maturity	1.94%	20,000,000.00
P503844	26/03/15	30/09/21	PWLB – for NHT	Maturity	2.09%	1,300,000.00
P504159	28/05/15	30/09/21	PWLB – for NHT	Maturity	2.36%	1,300,000.00
P504233	08/07/15	30/09/21	PWLB – for NHT	Maturity	2.46%	928,000.00
P504313	17/08/15	31/03/22	PWLB – for NHT	Maturity	2.47%	700,000.00
P504373	14/09/15	31/03/22	PWLB – for NHT	Maturity	2.36%	750,000.00
P504530	08/12/15	31/03/22	PWLB – for NHT	Maturity	2.31%	1,350,000.00
					4.18%	698,679,931.62
External borrowing average rate and total				**3.66%**		**£963,485,931.62**