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Governance Committee

Tuesday, 30th November, 2021, 6.00 pm

Shield Room, Civic Centre, West Paddock, Leyland PR25 1DH

Agenda

1	**Apologies for absence**	
2	**Declarations of Interest** Members are requested to indicate at this stage in the proceedings any items on the agenda in which they intend to declare an interest. Members are reminded that if the interest is a Disclosable Pecuniary Interest (as defined in the Members' Code of Conduct) they must leave the room for the whole of that item. If the interest is not a Disclosable Pecuniary Interest, but is such that a member of the public could reasonably regard it as being so significant that it is likely that it would prejudice their judgment of the public interest (as explained in the Code of Conduct) then they may make representations, but then must leave the meeting for the remainder of the item.	
3	**Minutes of meeting Wednesday, 29 September 2021 of Governance Committee** Minutes of the last meeting held, Wednesday 29 September 2021 are attached as a correct record for signing by the Chair.	(Pages 3 - 6)
4	**Audit Progress Report and Sector Update** Report of the External Auditors attached.	(Pages 7 - 24)
5	**Appointment of External Auditors** Report of the Director of Governance and Monitoring Officer attached.	(Pages 25 - 28)
6	**Treasury Management Activity Mid-Year Review 2021/22** Report of the Director of Finance attached.	(Pages 29 - 48)

Gary Hall
Chief Executive

Electronic agendas sent to Members of the Governance Committee Councillors Ian Watkinson (Chair), Colin Sharples (Vice-Chair), Damian Bretherton, Margaret Smith, Alan Ogilvie, Angela Turner and Kath Unsworth

Meeting contact Coral Astbury, Democratic and Member Services Officer or email coral.astbury@southribble.gov.uk

The minutes of this meeting will be available on the internet at www.southribble.gov.uk

Forthcoming Meetings
6.00 pm Tuesday, 25 January 2022 - Wheel Room, Civic Centre, West Paddock, Leyland PR25 1DH

Minutes of	**Governance Committee**
Meeting date	**Wednesday, 29 September 2021**
Members present:	Councillors Ian Watkinson (Chair), Colin Sharples (Vice-Chair), Damian Bretherton, Margaret Smith, Alan Ogilvie, Angela Turner and Kath Unsworth
Attended virtually:	Councillors Matthew Tomlinson and Carol Wooldridge, Matt Derrick (Grant Thornton PLC) and Georgia Jones (Grant Thornton PLC)
Officers present:	Gary Hall (Chief Executive), Chris Moister (Director of Governance), Louise Mattinson (Director of Finance and Section 151 Officer), Dawn Highton (Shared Service Lead- Audit & Risk), Tony Furber (Principal Financial Accountant), Darren Cranshaw (Shared Services Lead - Democratic, Scrutiny & Electoral Services), Coral Astbury (Democratic and Member Services Officer), Georgia Jones and Matt Derrick (Public Sector Audit Senior Manager)
Other attendees:	Councillor Paul Foster (Leader of the Council, Cabinet Member (Strategy and Reform) and Leader of the Labour Group), Councillor Phil Smith (Deputy Leader of the Opposition and Deputy Leader of the Conservative Group) and Councillor Karen Walton (Leader of the Opposition and Leader of the Conservative Group)
Public:	0

18 Apologies for absence

No apologies were received.

19 Declarations of Interest

There were no declarations of interest.

20 Minutes of meeting Tuesday, 27 July 2021 of Governance Committee

Resolved: (Unanimously)

That the minutes of the meeting held, Tuesday 27 July 2021 were agreed as a correct record for signing by the Vice-Chair.

21 Internal Audit Interim Report as at 31st August 2021

The Shared Service Lead (Audit and Risk) presented a report which advised the committee of the work undertaken in respect of the Internal Audit Plan from April 2021 to August 2021 and gave an appraisal of the Internal Audit Service's performance to date.

Members noted the information contained within the report relating to completed audits. It was advised that the Health and Wellbeing Campus report was appended to the report, having been presented in draft form in June 2020. Internal Audit had now reviewed all the evidence and re-drafted the report, although the findings were still the same the style in which the report had been presented has changed.

The Shared Service Lead (Audit and Risk) advised Members that the Internal Audit team were slightly below target in terms of their own performance indicators mainly due to the recruitment exercise taking longer than anticipated, although the team was now fully resourced. The service was also seeking reaccreditation of ISO9001 and are on track to be re-accredited in December 2021.

In response to a member enquiry, it was explained that when the plan is put together the service estimates how many days are needed to complete each audit. However, this can change dependant upon what is uncovered during the audit.

Members sought clarification on the accuracy of data held by Neighbourhoods and asked what impact this would have on other services across the council. In response, the Shared Service Lead (Audit & Risk) explained that the review had taken place following a request from the Director who had concerns about the data within the system. However, progress had already been made to identify assets and improve records, the data would be ready to migrate to the new system by April 2022.

Resolved: (Unanimously)

That the report be noted.

22 Audit Findings Report 2020/21

The Council's External Auditors presented a report which sought to provide members with the Audit Findings for the year ending 31 March 2021. Members were advised that three adjustments to the Statement of Accounts had been identified, with a further adjustment provided in the supplementary agenda. Members noted that following completion of the Audit Findings Report further areas such as, exit packages and queries surrounding fees and debtors had now been resolved. The External Auditors were also working with Officers to resolve any outstanding queries.

Members sought clarification on pension liabilities and asked if the £236,000 underpayment of the estimated upfront payment of pension costs for 2020/21, and the £831,000 pension liability following the transfer of staff from the South Ribble Community Leisure Trust (SRCLT,) would appear as an annual liability. In response, the External Auditor explained that the two issues were separate, and the £236,000 underpayment would not impact on the overall liability. Moving forwards the leisure centre liability would be part of that overall pension liability as the SRCLT staff would become council staff. The Director of Finance confirmed that provisions had been made for this within the relevant budget.

Members highlighted that the current letter of representation stated it would be approved on the 28 September 2021 and this would need amending to reflect the change in meeting date. The External Auditor confirmed they would re-issue the letter with the amended date and ensure all dates coincide for circulation.

Resolved: (Unanimously)

That the report be noted.

23 Audited Statement Of Accounts 2020/21

The committee considered the report of the Director of Finance which presented the Statement of Accounts for 2020/21 for approval. The Director of Finance explained that the committee had previously considered the unaudited statement of accounts in July 2021, this had been presented to the External Auditors and was back before committee for formal approval before the deadline of 30 September 2021.

Amendments had been made to the statement of accounts since it was considered in July 2021 as part of the further review and audit concluded by Grant Thornton. These adjustments had been summarised earlier in the meeting by the External Auditors.

Members commented that it was pleasing to see the pension fund investment increase substantially from £90 million to £99 million.

In response to a query, the External Auditor provided that their opinion would be given on Value for Money at the end of December, the opinion on the statement of accounts would be issued within the next couple of weeks. The draft opinion within the Audit Findings Report 2020/21 states an unqualified opinion would be issued. If any material changes were identified after the meeting, then a further report would be brought back to the next committee meeting.

Resolved: (Unanimously)

That the committee

1. Approve the audited Statement of Accounts for 2020/21 subject to any amendments which, in the opinion of the Chief Financial Officer (Section 151 Officer), are minor in nature. Such amendments are to be defined as non-material to the financial position of the authority. The Chief Financial Officer will exercise this delegation in consultation with the Chair of Governance Committee. In the event the Chief Financial Officer is of the opinion the amendments are material to the financial position of the authority, Governance Committee will be reconvened to approve the new Statement of Accounts.

2. Considers and approves the letter of representation contained at Appendix B and authorise the Chief Financial Officer and the Chair of Governance Committee to sign the letter.

Agenda Item 3

Chair Date

Grant Thornton

This version of the report is a draft. Its contents and subject matter remain under review and its contents may change and be expanded as part of the finalisation of the report.
This draft has been created from the template dated DD MMM YYYY

South Ribble Borough Council
Audit Progress Report and Sector Update

Year ending 31 March 2021

November 2021

Contents

The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit planning process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect the Authority or all weaknesses in your internal controls. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

Introduction

Your key Grant Thornton team members are:

Georgia Jones
Key Audit Partner
T 0161 214 6383
E Georgia.S.Jones@uk.gt.com

Matt Derrick
Senior Manager
T 0141 223 0656
E Matt.F.Derrick@uk.gt.com

Nicole Doroja
Senior In-charge Auditor
T 0117 305 7600
E Nicole.Aira.Doroja@uk.gt.com

This paper provides the Governance Committee with a report on progress in delivering our responsibilities as your external auditors.

The paper also includes:

- a summary of emerging national issues and developments that may be relevant to you as a local authority; and
- includes a number of challenge questions in respect of these emerging issues which the Committee may wish to consider (these are a tool to use, if helpful, rather than formal questions requiring responses for audit purposes)

Members of the Governance Committee can find further useful material on our website, where we have a section dedicated to our work in the public sector. Here you can download copies of our publications www.grantthornton.co.uk ..

If you would like further information on any items in this briefing, or would like to register with Grant Thornton to receive regular email updates on issues that are of interest to you, please contact either your Engagement Lead or Engagement Manager.

Progress at November 2021

Financial Statements Audit

We undertook our initial planning for the 2020/21 audit in April 2021. We began our work on your draft financial statements in July 2021.

In July we issued a detailed audit plan, setting out our proposed approach to the audit of the Authority's 2020/21 financial statements.

The Accounts and Audit (Amendment) Regulations 2021 push back the date by which principal authorities need to publish their draft financial statements to the first working day of August. In 2020 this date was pushed back to 31 August. The date by which authorities are required to publish audited financial statements is 30 September. In 2020 this date was pushed back to 30 November.

We have completed our work on the Council's financial statements and reported on this work to the Governance Committee in our Audit Findings Report on 29 September. We issued an unqualified opinion on the Council's financial statements on 5 November 2021.

We are continuing with our value for money work and will report to committee members on the outcome of that work in our Auditor's Annual Report. This is due by 5 February 2022.

Value for Money

The new Code of Audit Practice (the "Code") came into force on 1 April 2020 for audit years 2020/21 and onwards. The most significant change under the new Code is the introduction of an Auditor's Annual Report, containing a commentary on arrangements to secure value for money and any associated recommendations, if required.

The new approach is more complex, more involved and is planned to make more impact.

Under the 2020 Code of Audit Practice, for relevant authorities other than local NHS bodies auditors are required to issue our Auditor's Annual Report no later than 30 September or, where this is not possible, issue an audit letter setting out the reasons for delay.

As a result of the ongoing pandemic, and the impact it has had on both preparers and auditors of accounts to complete their work as quickly as would normally be expected, the National Audit Office has updated its guidance to auditors to allow us to postpone completion of our work on arrangements to secure value for money and focus our resources firstly on the delivery of our opinions on the financial statements. This is intended to help ensure as many as possible could be issued in line with national timetables and legislation. The extended deadline is now no more than three months after the date of the opinion on the financial statements.

Progress at November 2021 (cont.)

Other areas

Certification of claims and returns

We certify the Authority's annual Housing Benefit Subsidy claim in accordance with procedures agreed with the Department for Work and Pensions (DwP). The certification work for the 2020/21 claim is due to begin in December with the deadline for the completed certification being 31 January 2022.

Meetings

We meet with Finance Officers on a regular basis and continue to be in discussions with finance staff regarding emerging developments and to ensure the audit process is smooth and effective. We also met with your Chief Executive and Senior Leadership Team in November to discuss the Authority's strategic priorities and plans.

Events

We provide a range of workshops, along with network events for members and publications to support the Authority. Your officers attended our Financial Reporting Workshop in February, which helped to ensure that members of your Finance Team were up to date with the latest financial reporting requirements for local authority accounts.

Further details of the publications that may be of interest to the Authority are set out in our Sector Update section of this report

Audit Fees

During 2017, PSAA awarded contracts for audit for a five year period beginning on 1 April 2018. 2020/21 is the third year of that contract. Since that time, there have been a number of developments within the accounting and audit profession. Across all sectors and firms, the Financial Reporting Council (FRC) has set out its expectation of improved financial reporting from organisations and the need for auditors to demonstrate increased scepticism and challenge and to undertake additional and more robust testing.

Our work in the Local Government sector in 2018/19 and 2019/20 has highlighted areas where financial reporting, in particular, property, plant and equipment and pensions, needs to improve. There is also an increase in the complexity of Local Government financial transactions and financial reporting. This combined with the FRC requirement that all Local Government audits are at or above the "few improvements needed" (2A) rating means that additional audit work is required.

We have reviewed the impact of these changes on both the cost and timing of audits. We have discussed this with your s151 Officer including any proposed variations to the Scale Fee set by PSAA Limited, and have communicated fully with the Governance Committee in our audit plan.

As a firm, we are absolutely committed to meeting the expectations of the FRC with regard to audit quality and local government financial reporting.

Audit Deliverables

2020/21 Deliverables	Planned Date	Status
Audit Plan We are required to issue a detailed audit plan to the Governance Committee setting out our proposed approach in order to give an opinion on the Authority's 2020/21 financial statements and the Auditor's Annual Report on the Authority's Value for Money arrangements.	July 2021	Complete
Audit Findings Report The Audit Findings Report was reported to the September Governance Committee.	September 2021	Complete
Auditors Report This is the opinion on your financial statements.	November 2021	Complete
Auditor's Annual Report This Report communicates the key issues arising from our Value for Money work.	February 2022	Not yet due

Sector Update

Authorities continue to try to achieve greater efficiency in the delivery of public services, whilst facing the challenges to address rising demand, ongoing budget pressures and social inequality.

Our sector update provides you with an up to date summary of emerging national issues and developments to support you. We cover areas which may have an impact on your organisation, the wider local government sector and the public sector as a whole. Links are provided to the detailed report/briefing to allow you to delve further and find out more.

Our public sector team at Grant Thornton also undertake research on service and technical issues. We will bring you the latest research publications in this update. We also include areas of potential interest to start conversations within the organisation and with audit committee members, as well as any accounting and regulatory updates.

- Grant Thornton Publications
- Insights from local government sector specialists
- Reports of interest
- Accounting and regulatory updates

More information can be found on our dedicated public sector and local government sections on the Grant Thornton website by clicking on the logos below:

Public Sector

Local government

The new approach to Value for Money

The nature of value for money work

Section 20 and 21 of the Local Audit and Accountability Act 2014 (the Act), require auditors to be satisfied that the body "has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources". The auditor's work on VFM arrangements is undertaken in accordance with the Code and its supporting statutory guidance. The Comptroller and Auditor General has determined through the 2020 Code and guidance that the key output from local audit work in respect of VFM arrangements is the commentary as reported in the Auditor's Annual Report. It is therefore not a VFM arrangements 'conclusion' or an 'opinion' in the same sense as the opinion on the financial statements themselves. The Act and the Code require auditors to consider whether the body has put in place 'proper arrangements' for securing VFM. The arrangements that fall within the scope of 'proper arrangements' are set out in 'AGN 03 Auditors' work on VFM arrangements', which is issued by the NAO. When reporting on these arrangements, the Code requires auditors to structure their commentary on arrangements under three specified reporting criteria:

Financial sustainability

How the body plans and manages its resources to ensure it can continue to deliver its services, including how the body:

- ensures that it identifies all the significant financial pressures that are relevant to its short and medium-term plans and builds these into them;
- plans to bridge its funding gaps and identifies achievable savings;
- plans finances to support the sustainable delivery of services in accordance with strategic and statutory priorities;
- ensures that its financial plan is consistent with other plans such as workforce, capital, investment, and other operational planning which may include working with other local public bodies as part of a wider system; and
- identifies and manages risks to financial resilience, e.g. unplanned changes in demand, including challenge of the assumptions underlying its plans.

Governance

How the body ensures that it makes informed decisions and properly manages its risks, including how the body:

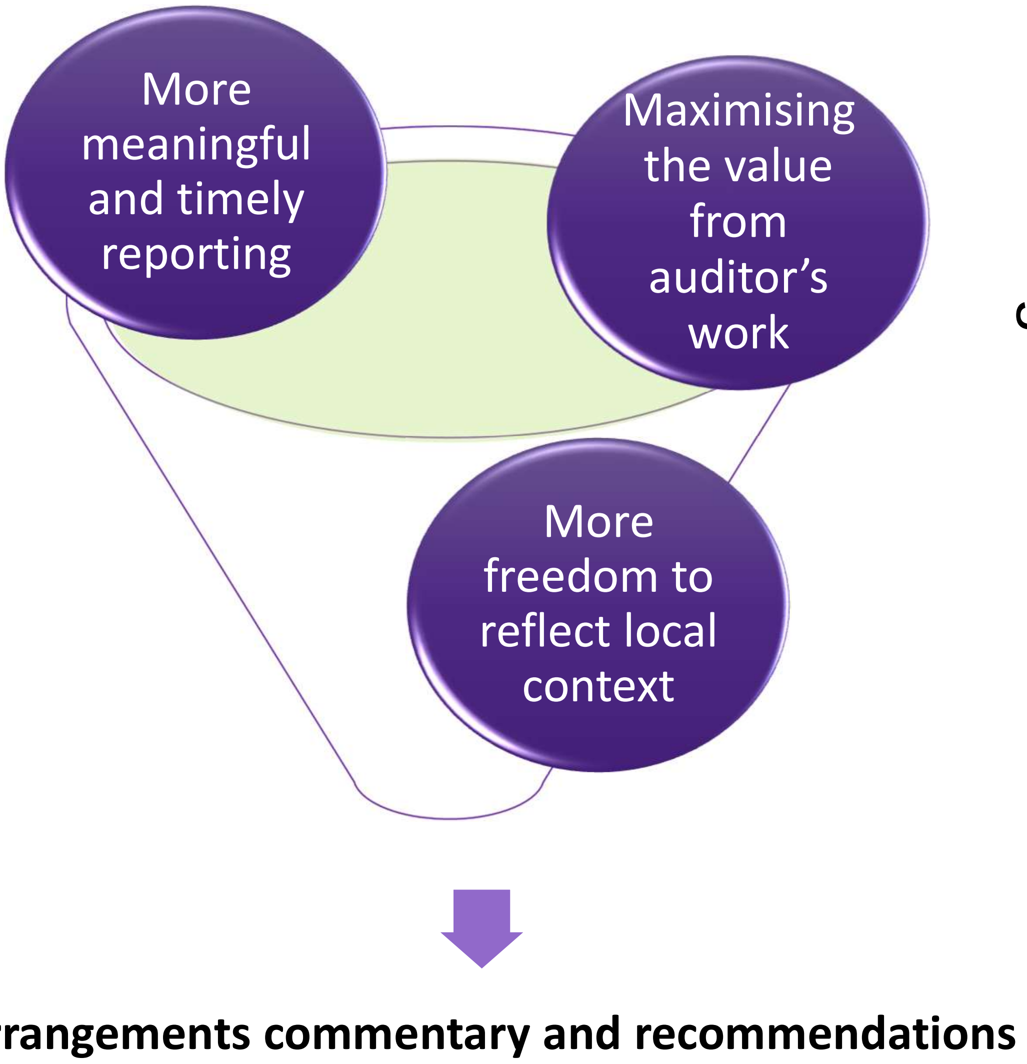
- monitors and assesses risk and how the body gains assurance over the effective operation of internal controls, including arrangements to prevent and detect fraud;
- approaches and carries out its annual budget setting process;
- ensures effective processes and systems are in place to ensure budgetary control; to communicate relevant, accurate and timely management information (including non-financial information where appropriate); supports its statutory financial reporting requirements; and ensures corrective action is taken where needed;
- ensures it makes properly informed decisions, supported by appropriate evidence and allowing for challenge and transparency. This includes arrangements for effective challenge from those charged with governance/audit committee; and
- monitors and ensures appropriate standards, such as meeting legislative/regulatory requirements and standards in terms of officer or member behaviour (such as gifts and hospitality or declarations/conflicts of interests).

The new approach to Value for Money

Improving economy, efficiency and effectiveness

How the body uses information about its costs and performance to improve the way it manages and delivers its services, including:

- how financial and performance information has been used to assess performance to identify areas for improvement;
- how the body evaluates the services it provides to assess performance and identify areas for improvement;
- how the body ensures it delivers its role within significant partnerships, engages with stakeholders it has identified, monitors performance against expectations, and ensures action is taken where necessary to improve; and
- where the body commissions or procures services, how the body ensures that this is done in accordance with relevant legislation, professional standards and internal policies, and how the body assesses whether it is realising the expected benefits.



The new approach to Value for Money

The table below details what will be reported in the Auditor's Annual Report:

Section of report	Content
Commentary on arrangements	An explanation of the VFM work that has been undertaken during the year, including the risk assessment and any further risk-based work. It will also highlight any significant weaknesses that have been identified and brought to the body's attention. The commentary will allow auditors to better reflect local context and draw attention to emerging or developing issues which may not represent significant weaknesses, but which may nevertheless require attention from the body itself.
Recommendations	Where an auditor concludes that there is a significant weakness in a body's arrangements, they report this to the body and support it with a recommendation for improvement.
Progress in implementing recommendations	Where an auditor has reported significant weaknesses in arrangements in the previous year, the auditor should follow up recommendations issued previously and include their view as to whether the recommendations have been implemented satisfactorily.
Use of additional powers	Where an auditor uses additional powers, such as making statutory recommendations or issuing a public interest report, this should be reported in the auditor's annual report.
Opinion on the financial statements	The auditor's annual report also needs to summarise the results of the auditor's work on the financial statements.

The table below details the three types of recommendations that auditors can make. Auditors may make recommendations at any time during the year.

Type of recommendation	Definition
Statutory recommendation	Where auditors make written recommendations to the body under Section 24 and Schedule 7 of the Local Audit and Accountability Act 2014. A recommendation of this type requires the body to discuss and respond publicly to the report.
Key recommendation	Where auditors identify significant weaknesses in a body's arrangements for securing value for money, they have to make recommendations setting out the actions that the body should take to address them
Improvement recommendation	Where auditors do not identify a significant weakness in the body's arrangements, but still wish to make recommendations about how the body's arrangements can be improved

What can be learned from Public Interest Reports?– Grant Thornton

2020 will be remembered as a tumultuous year in local government, with the pandemic creating unprecedented pressure on the sector. It also saw the appearance of two Public Interest Reports (PIRs), followed by another in January this year – the first to be issued in the sector since 2016. PIR's can be issued by local auditors if there are significant concerns around council activity, such as major failings in finance and governance.

The recent PIRs have made headlines because, up to this point, very few have ever been issued. But, as our latest report "Lessons from recent Public Interest Reports" explores, all three illustrate some of the fundamental issues facing the wider sector and provide a lesson for all local authorities around: weaknesses in financial management; governance and scrutiny practices; and council culture and leadership; which, when combined, can provide fertile ground for the kind of significant issues we might see in a PIR.

The COVID-19 pandemic highlighted four essential factors we probably always knew about local government, have often said, but which are now much better evidenced:

1) Local government has provided fantastic support to its communities in working with the NHS and other partners to deal with the multifaceted challenges of the pandemic.
2) Britain's long centralised approach to government has been exposed to some degree in terms of its agility to tailor pandemic responses to regional and local bodies. This is recognised by the current government who continue to pursue the options for devolution of powers to local bodies. Track and Trace delivered centrally has not been as successful as anticipated and, according to government figures, local interventions have had more impact.
3) Years of reduced funding from central government have exposed the underlying flaws in the local authority business model, with too much reliance on generating additional income.
4) Not all authorities exercise appropriate care with public money; not all authorities exercise appropriate governance; and not all authorities have the capability of managing risk, both short and long term. Optimism bias has been baked into too many councils' medium-term plans.

The PIRs at Nottingham City Council (August 2020), the London Borough of Croydon (October 2020), and Northampton Borough Council (January 2021) are clear illustrations of some of the local government issues identified above. The audit reports are comprehensive and wide-ranging and a lesson for all local authorities. Local authorities have a variety of different governance models. These range from elected mayor to the cabinet and a scrutiny system approach, while others have moved back to committee systems. Arguments can be made both for and against all of these models. However, in the recent PIR cases, and for many other local authorities, it's less about the system of governance and more about how it operates, who operates it and how willing they are to accept scrutiny and challenge.

There are a number of lessons to be learned from the recent PIR reports and these can be broken down into three key areas which are explored further in our report:

1) The context of local government in a COVID-19 world
2) Governance, scrutiny, and culture
3) Local authority leadership.

The full report is available here:

[Lessons from recent Public Interest Reports | Grant Thornton]

Annual Transparency Report – Grant Thornton

As auditors of several listed entities as well as nearly one hundred major local audits, we are required as a firm to publish an annual transparency report.

The report contains a variety of information which we believe is helpful to audit committees as well as wider stakeholders. The Financial Reporting Council (FRC) in their thematic review of transparency reporting noted that they are keen to see more Audit Committee Chairs actively engaging and challenging their auditors on audit quality based on the information produced in Transparency reports on a regular basis. We agree with the FRC and are keen to share our transparency report and discuss audit quality with you more widely.

The transparency report provides details of our:

- Leadership and governance structures
- Principle risks and Key Performance Indicators
- Quality, risk management and internal control structure
- Independence and ethics processes
- People and culture
- Compliance with the Audit Firm Governance code and EU Audit directive requirements

We have made significant developments in the year as part of our Local Audit Investment Plan to improve our audit quality. We welcome an opportunity to discuss these developments and our transparency report should you wish.


Grant Thornton

Transparency report

Grant Thornton UK LLP year ending 31 December 2020

April 2021

The full report is available here:

Transparency report 2020 (grantthornton.co.uk)

Local authority Covid-19 pressures – MHCLG

Outturn figures from the Ministry for Housing, Communities and Local Government (MHCLG) show that local authorities in England reported additional cost pressures of £12.8bn relating to Covid-19 in 2020-21. Overall, local authorities spent £7.2bn responding to the pandemic last year, with the largest share of additional expenditure going on adult social care services at £3.2bn.

Additional expenditure due to COVID-19 by class and service area (£ millions) (2020-21)

	Shire District	Shire County	Unitary Authority	Metropolitan District	London Borough	Total
Adult Social Care – total	0.473	1,254.880	848.656	663.404	413.842	**3,181.254**
Children's social care - total (excluding SEND)	0.000	94.933	131.127	89.799	62.987	**378.846**
Housing - total (including homelessness services) excluding HRA	63.129	5.254	74.949	42.281	112.971	**298.584**
Environmental and regulatory services - total	33.564	68.097	67.512	66.704	63.556	**299.433**
Finance & corporate services - total	48.222	53.445	83.984	76.923	78.284	**340.858**
All other service areas not listed in rows above	184.550	634.578	584.924	564.737	395.137	**2,363.926**
Total	**329.937**	**2,111.187**	**1,791.153**	**1,503.848**	**1,126.777**	**6,862.902**

Income losses due to COVID-19 by class and source of income (£ millions) (2020-21)

	Shire District	Shire County	Unitary Authority	Metropolitan District	London Borough	Total
Business rates	276.498	0.000	194.192	207.351	537.667	**1,215.708**
Council tax	399.037	0.000	217.633	191.219	232.727	**1,040.616**
Sales fees and charges	516.426	194.923	553.907	396.745	475.728	**2,137.728**
Commercial income	82.448	24.159	120.629	204.211	52.154	**483.600**
Other	33.494	39.947	27.163	53.664	45.166	**199.435**
Total	**1,307.903**	**259.029**	**1,113.524**	**1,053.190**	**1,343.441**	**5,077.087**

Ministry of Housing, Communities & Local Government

The figures are available in full here: https://www.gov.uk/government/publications/local-authority-covid-19-financial-impact-monitoring-information

Agenda Item 4

Government response to Redmond review – MHCLG

Government has published an update on the Ministry of Housing, Communities & Local Government response to Sir Tony Redmond's independent review into the effectiveness of external audit and transparency of financial reporting in local authorities.

The MHCLG press release states "The Audit, Reporting and Governance Authority (ARGA) – the new regulator being established to replace the Financial Reporting Council (FRC) – will be strengthened with new powers over local government audit, protecting public funds and ensuring councils are best serving taxpayers.

The new regulator, which will contain a standalone local audit unit, will bring all regulatory functions into one place, to better coordinate a new, simplified local audit framework.

ARGA will continue to act as regulator and carry out audit quality reviews as the FRC does now. It will now also provide annual reports on the state of local audit and take over responsibility for the updated Code of Local Audit Practice – the guidelines councils are required to follow.

The government has confirmed that the Public Sector Audit Appointments (PSAA) will continue as the appointing body for local audit, in charge of procurement and contract management for local government auditors.

In the immediate term, MHCLG will set up and chair a Liaison Committee, which will comprise senior stakeholders across the sector that will oversee the governance of the new audit arrangements and ensure they are operating effectively."

The press release goes on to state the "measures finalise the government's response to Sir Tony Redmond's independent review into local audit, carried out last year.

The government has already announced £15 million to support councils with additional costs in audit fees, and recently consulted on the distribution of this funding. Government is also consulting on improving flexibility on audit fee setting and has extended the deadline for when councils must publish their audited accounts.

The press release can be found here:

https://www.gov.uk/government/news/government-publishes-update-to-audit-review-response

2019/20 audited accounts – Public Sector Audit Appointments

In December 2020 Public Sector Audit Appointments (PSAA) published figures relating to the audit of 2019/20 local authority financial statements.

PSAA report "Audit arrangements in local councils, police, fire and other local government bodies are continuing to exhibit signs of stress and difficulty. In the latest audit round, focusing on 2019/20 financial statements and value for money arrangements, fewer than 50% of bodies' audits were completed by the revised target of 30 November.

Figures compiled by PSAA, the organisation responsible for appointing auditors to 478 local bodies, reveal that 55% (265) of audit opinions were not issued by 30 November. This is a further deterioration on 2018/19 audits when 43% of opinions (210 out of 486) were delayed beyond the then target timetable of 31 July."

By 30 November, Grant Thornton had signed 113/208 audits (a 55% completion rate), meaning that only 45% of audit opinions were not signed by 30 November, compared to the 55% all firms average.

PSAA go on to note "This year's timetable has been deliberately eased by Ministers in recognition of the underlying pressures on the audit process and the significant added complications arising from the Covid-19 pandemic. The pandemic has posed practical challenges for bodies in producing accounts and working papers, and for auditors to carry out their testing. Both sets of staff have had to work remotely throughout the period, and the second national lockdown came at a critical point in the cycle.

Questions and concerns about the potential implications of the pandemic for some bodies have meant that both finance staff and auditors have needed to pay particular attention to the financial position of each entity. Additionally, following a series of increasingly challenging regulatory reviews, auditors have arguably been more focused than ever on their professional duty to give their opinion only when they are satisfied that they have sufficient assurance."

The news article can be found here:

[News release: 2019/20 audited accounts – PSAA]

Consultation on 2023-24 audit appointments – Public Sector Audit Appointments

Public Sector Audit Appointments (PSAA) is consulting on the Draft prospectus for 2023 and beyond.

PSAA state "Our primary aim is to secure the delivery of an audit service of the required quality for every opted-in body at a realistic market price and to support the drive towards a long term competitive and more sustainable market for local public audit services.

The objectives of the procurement are to maximise value for local public bodies by:

- securing the delivery of independent audit services of the required quality;
- awarding long term contracts to a sufficient number of firms to enable the deployment of an appropriately qualified auditing team to every participating body;
- encouraging existing suppliers to remain active participants in local audit and creating opportunities for new suppliers to enter the market;
- encouraging audit suppliers to submit prices which are realistic in the context of the current market;
- enabling auditor appointments which facilitate the efficient use of audit resources;
- supporting and contributing to the efforts of audited bodies and auditors to improve the timeliness of audit opinion delivery; and
- establishing arrangements that are able to evolve in response to changes to the local audit framework."

The plans include proposals to adjust the procurement ratio between quality and costs from an equal 50:50 to 80:20, as well as trying to bring new suppliers in to the market.

The consultation on the PSAA's proposals closes on 8 July.

The news article can be found here: https://www.psaa.co.uk/about-us/appointing-person-information/appointing-period-2023-24-2027-28/prospectus-2023-and-beyond/draft-prospectus-for-2023-and-beyond/page/7/

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Agenda Item 4

Councils given power to build more homes for first time buyers and for social rent – MHCLG

The Ministry of Housing, Communities & Local Government (MHCLG) has announced that councils in England will have more freedom on how they spend the money from homes sold through Right to Buy to help them build the homes needed in their communities.

The MHCLG press release states the "package will make it easier for councils to fund homes using Right to Buy receipts, including homes for social rent, and give them greater flexibility over the types of homes they provide to reflect the needs of their communities.

It will also give councils more time to use receipts and to develop ambitious building programmes. The government wants homes supplied using Right to Buy receipts to be the best value for money, and to add to overall housing supply, to help towards delivering 300,000 new homes a year across England by the mid-2020s."

The press release goes on to note "New measures include:

- extending the time councils have to spend Right to Buy receipts from 3 years to 5 years
- increased cap on the percentage cost of new homes councils can fund from Right to Buy receipts raised from 30% to 40% per home, making it easier to build replacement homes
- allowing receipts to be used for shared ownership, First Homes, as well as affordable and social housing, to help councils build the homes their communities need
- introducing a cap on the use of Right to Buy receipts for acquisitions to help drive new supply."

Ministry of Housing, Communities & Local Government

The press release can be found here: https://www.gov.uk/government/news/councils-given-power-to-build-more-homes-for-first-time-buyers-and-for-social-rent

Grant Thornton

grantthornton.co.uk

Agenda Item 5

South Ribble Borough Council

Report of	Meeting	Date
Director of Governance and Monitoring Officer	Governance Committee	Tuesday, 30 November 2021

Appointment of External Auditors

Is this report confidential?	No

Is this decision key?	No

Purpose of the Report

1. The purpose of this report is to set out the options available to the Council for the appointment of an external auditor for the period 2023/24 to 2027/28.

Recommendations to Governance Committee

2. The committee is asked to recommend to Council to opt into the Public Sector Audit Appointments national scheme for the appointment of the external auditor.

Corporate priorities

3. The report relates to the following corporate priorities: (please bold all those applicable):

An exemplary council	Thriving communities
A fair local economy that works for everyone	Good homes, green spaces, healthy places

Background and Future Arrangements

4. A relevant authority must appoint an external auditor to audit its accounts. The Council can either appoint its external auditor directly or an “appointing person” can make the appointment on the Council’s behalf. The only “appointing person” is the Public Sector Audit Appointments Limited (PSAA) who are a not for profit organisation.

5. Following the abolition of the Audit Commission, the Council took advantage of the national collective scheme administered by the PSAA for the appointment of its external auditors for the five years commencing 1st April 2018.

6. The second appointing period is to span the five consecutive financial years commencing 1 April 2023 and cover the audit of account for the financial years 2023/24 to 2027/28.

7. The Council is required to appoint an external auditor by 31 December 2022 to commence 1 April 2023. There are three options available for appointing its external auditor:

   Option 1

   Establish its own independent auditor panel under part 3, section 9 and schedule 4 of the Local Audit and Accountability Act 2014. The panel must be made up of a majority, or of wholly independent members and must be chaired by an independent member. It would therefore be necessary to undertake a selection process to appoint the panel, whose members may be remunerated. The panel's role would be to advise the council on the selection of its external auditor and therefore to oversee a procurement process.

   Option 2

   Establish a joint independent auditor panel to carry out the function on behalf of two or more councils which would therefore have to agree on the selection criteria firstly for the panel's members and then for the external auditor, and then oversee a procurement process.

   Option 3

   Opt into PSAA's sector led national scheme. Legislation requires a resolution of Full Council if a local authority wishes to opt into the new national arrangement. No significant further action would then be required by the Council.

8. On 22 September 2021 PSAA invited all principal local government bodies to become opted-in authorities. Eligible bodies have until 11 March 2022 to formally respond and accept the opt-in invitation.

9. The national scheme is considered to represent the best option as the Council will benefit from PSAA's experience of working within the context of the Regulations to appoint auditors, manage contracts with audit firms, setting and determining audit fees. It avoids the necessity to establish an independent auditor panel and undertake a procurement exercise and assures the independence of the auditor's appointment for the council.

Comments of the Statutory Finance Officer

10. Efficiencies and economies of scale should be obtained by opting-in to the procurement exercise to be undertaken by PSAA, who will do so on behalf of many councils across the country, rather than trying to procure in isolation, or with another/several other council(s).

11. There are only a limited number of external audit firms who have the capacity and specialist teams to undertake local authority audits and therefore there is a risk that in

trying to procure in isolation/in a small group, we may get a low level of interest, and/or higher cost, as the external audit firms would be likely to focus their efforts in securing a larger contract through the PSAA procurement exercise.

Comments of the Monitoring Officer

12. The report clearly sets out what the options are. If Governance Committee is minded to opt for the national scheme referred to then a decision of Full Council will be required.

Report Author:	Email:	Telephone:	Date:
Dawn Highton (Shared Service Lead- Audit & Risk)	dawn.highton@southribble.gov.uk	01772 625625	16/11/21

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Agenda Item 6

Report of	Meeting	Date
Director of Finance and Section 151 Officer	Governance Committee	Tuesday, 30 November 2021

Treasury Management Activity Mid-Year Review 2021/22

Is this report confidential?	No

Is this decision key?	No

Purpose of the Report

1. To report on Treasury Management performance in financial year 2021/22 to the end of September.

Recommendations to Governance Committee

2. That the report be noted.

Corporate priorities

3. The report relates to the following corporate priorities: (please bold all those applicable):

An exemplary council	Thriving communities
A fair local economy that works for everyone	Good homes, green spaces, healthy places

Background to the report

4. The Annual Investment Strategy for 2021/22 was included in the Treasury Strategy 2021/22 to 2023/24, which was approved by Council on 24 February 2021. The report emphasised that the Council's investment priorities will be Security first, portfolio Liquidity second, and only then return (Yield).

5. The Treasury Management Annual Report 2020/21 was presented to Governance Committee on 27 July 2021. The report indicated that an average return on investments of 0.36% had been achieved, which exceeded the target rate of 0.10%.

6. The Code of Practice for Treasury Management requires councils to review their treasury strategies and activities half yearly. This report satisfies that requirement.

Treasury Activity

7. Investment activity up to the end of September 2021 is summarised in the following table.

Table 1 - Investment Activity	Average Daily Investment £000	Earnings to 30 September 2021 £	Average Rate %
Debt Management Office	8,877	445	0.01
Other fixed term deposits	15,000	14,022	0.19
Notice Accounts	12,000	13,838	0.23
Call accounts	3,400	520	0.03
Money Market Funds	14,922	673	0.01
Total	**54,199**	**29,498**	**0.11%**

8. Given the low (even compared to those more generally available) rates of interest available from the Debt Management Office, this counterparty is usually used only rarely, when the amounts that need to be kept at short notice are greater than what can be accommodated within the approved counterparty limits. However, during the first half of 2021/22, as for 2020/21, the continuing impacts of the Covid 19 pandemic have had an ongoing effect on the Council's cash flows with significant Covid funding received from central government for onward payment e.g. in the form of Business Grant payments. As this was the case for all councils across the country, there was little demand for councils to borrow, and so for us to place deposits with them as we have done in the past. As a result, larger and more frequent amounts were placed with the Debt Management Office than would normally be the case.

9. The average daily investment of £54.199m continues to be well above the £10m minimum balance invested for the Council to qualify as a professional investor under MiFID II requirements. As noted above, because of the ongoing impacts of cash flows resulting from the Covid 19 pandemic, balances during the year to date have been higher than would otherwise have been the case.

10. A full list of investment counterparties and their associated limits is shown at Appendix A.

11. A full list of investments as at 30 September 2021 is presented as Appendix B. All investments throughout the first six months of the year were within the maximum limits per counterparty permitted by the approved Investment Strategy for 2021/22.

12. The investment durations per bank or building society suggested by Link Asset Services as at November 2021 are presented in Appendix C. The Council receives weekly updates, and suggested durations are checked online at the time of placing any term deposits with banks or building societies. The limit per institution is as approved by Council on 24 February 2021.

13. The average interest earned of 0.11% would normally be measured against a target of the average LIBID 7-day rate plus 15%, but the exceptional market conditions applying in

2020/21 mean that this would produce a negative target figure. Link Asset Services have therefore produced the following table of benchmark returns. That actually achieved by the Council have exceeded these targets. It also exceeds the Link Asset Services suggested earnings rate of 0.10% for 2021/22 (see Table 4 below).

14. The standard target against which investment earnings would previously have been measured is the average LIBID 7-day rate plus 15%, However, the continuing exceptional market conditions applying in the first half of 2021/22 have meant that the LIBID based calculation has produced a negative target figure, as shown in Table 3 below. Link Asset Services have therefore produced a replacement set of benchmark returns, based on a wider view of the market conditions (see Table 4, at paragraph 22). This shows a target of 0.1% for 2021/22.

Table 2 - Benchmark Investment Rates	
Period	**Benchmark Return**
7 day	-0.08%
1 month	-0.07%
3 months	-0.05%
6 months	-0.02%
12 months	0.07%

15. Performance is expected to continue at or around the same levels throughout the rest of year and the forecast outturn position for interest earned, as contained in the revenue monitoring report received by Cabinet on 17 November 2021, is shown in Table 3 below.

Table 3 - Interest Receivable Budget	**Budget for 2021/22 £000**	**Actual to 30 September 2021 £000**	**Forecast for year £000**
Interest earned	118	29	55
Total	**200**	**141**	**185**

16. No long-term borrowing has been undertaken in the first six months of 2021/22. The funding of the Capital Programme for the year requires an element of long-term borrowing and the cost of financing this has been included in the revenue budget for the year. Savings in interest payable may be achieved by delaying external borrowing, or by using the Council’s cash balances as an alternative to taking external loans from the Public Works Loan Board (PWLB) or other sources. Interest earned on cash balances would reduce as a consequence, but the Council would lose interest receivable at approximately 0.10% to 0.20%, while avoiding the relatively higher cost of paying interest to an external lender. For example, the rate on a 40-year annuity loan from the PWLB on 22 November 2021 was 1.94%.

17. No rescheduling of debt has been undertaken in the first six months of the year.

18. All activities in the first half of the year complied with the approved prudential indicators.

Treasury Consultants Advice

19. Appendix D presents the advice of Link Asset Services in respect of economic matters and interest rates in the first half of 2021/22.

20. In addition, a detailed comparison of interest rate forecasts is presented at Appendix E. Bank rate and PWLB borrowing rate forecasts are given from the December quarter of 2021 through to the March quarter of 2025.

21. The Bank Rate is now forecast to rise from its current level of 0.10% to 0.25% by the end of December 2021, before rising steadily to 1.25% by March 2025.

22. Link's suggested budgeted investment earning rates for investments of up to about three months duration in each financial year are as follows:

Table 4 - Average Earnings in each financial year			
	Revised November 2021	**Revised September 2021**	**Original February 2021**
2021/22	N/A	0.10%	0.10%
2022/23	0.50%	0.25%	0.10%
2023/24	0.75%	0.50%	0.10%
2024/25	1.00%	0.50%	0.20%
2025/26	1.25%	1.00%	N/A
Later years	2.00%	2.00%	2.25%

23. The most recent estimate is compared to the estimated earnings rate available at the time the Treasury Management Strategy was presented for approval in February 2021, and Link's update in September 2021. The suggested earnings rates for the current year have remained unchanged at 0.10%, with any rises in rates not expected to have an impact until late in the year.

Peer Review

24. In the recent Corporate Peer Challenge of the council, led by the Local Government Association (LGA) over the summer, reference was made to Treasury Management activities in two areas:

    a) *'The peer team heard a range of views from across political groups regarding these financial issues and would encourage the use of external training to support informed political debate on issues such as Treasury Management, CIPFA consultation responses and capital financing to facilitate this. This training will also help to ensure that there is a shared understanding of the council's financial context across the organisation and support a more dispersed ownership of financial management.'*

ACTION: - Training is being arranged for delivery over the next 2-3 months by specialist, Treasury Management consultants to address this recommendation.

b) *Whilst the Treasury Management Strategy has been reviewed; the council is risk averse around its counterparty listing and it has been stated that the policy was implemented following the collapse of the Icelandic Banks. The peer team would therefore invite the council to discuss alternative investments over longer time periods with Link Asset Management* (the council's Treasury Management Advisors) *to explore whether higher levels of investment income could be received whilst mitigating risk.*

ACTION: - Discussions have begun with Link in response to the comment from the peer review team above. Link have reviewed the council's Treasury Management Strategy and have stated that they believe this is flexible enough and that the approach taken is consistent with that of many councils in prioritising security and liquidity of investment over yield. They have noted that during the pandemic the amount of cash received by councils from central government has been unprecedented, and the need to access this has been less predictable than is usually the case. Going forward however, they believe there is opportunity to increase returns by investing some sums for longer periods of time; we shall seek to develop this approach in line with the council's Treasury Management Strategy and Prudential Indicators.

Climate change and air quality

25. The work noted in this report does not impact the climate change and sustainability targets of the Councils Green Agenda and all environmental considerations are in place.

Equality and diversity

26. This report has no implications in respect of equality and diversity.

Risk

27. There are a number of risks inherent to treasury management activities, both in the security of any investments placed and in managing both investments and borrowing based on actual and forecast interest rates. The Council's treasury management strategy and policies are designed to ensure the effective control and management of the risks associated with such activities and this report forms part of that overall framework.

Comments of the Statutory Finance Officer

28. This report complies with the statutory requirement to review treasury strategies and activities half yearly.

Comments of the Monitoring Officer

29. The Monitoring Officer has no comments.

Background documents

Treasury Management Strategy 2021/22 to 2023/24 (Council 24 February 2021)

Appendices

Appendix A Investment Counterparties
Appendix B List of Investments as at 30 September 2019
Appendix C Suggested Investment Durations as at November 2019
Appendix D Economics and Interest Rates – Treasury Advisors' advice
Appendix E Comparison of Interest Rates Forecasts

Report Author:	Email:	Telephone:	Date:
Tony Furber (Principal Financial Accountant)	tony.furber@southribble.gov.uk	01257 515025	22 November 2021

APPENDIX A

Investment Counterparties 2020/21

Category	Institutions	LAS Colour Code	Maximum Period	Limit per Institution
Banks & Building Societies: Call Accounts /Term Deposits / Certificates of Deposit (CDs)				
Government related/guaranteed	DMADF (DMO) UK Local Authority	Yellow Yellow	6 months 2 years	Unlimited £6m per LA
UK part-nationalised institutions	Royal Bank of Scotland group	Blue	1 year	£6m per group
UK-incorporated Institutions	UK banks and building societies of high credit quality	Orange Red Green	1 year 6 months 3 months	£6m per group (or independent institution)
Non-UK Banks	Non-UK banks of high credit quality	Orange Red Green	1 year 6 months 3 months	£4m per group (or independent institution); £8m in total for this category
Money Market Funds				
Money Market Funds	MMFs of high credit quality - AAA rated		Instant access	£5m per fund

There are no changes from the Investment Counterparties list approved by Council as part of the Treasury Management Strategy 2021-22 to 2023-24 on 24 February 2021.

APPENDIX B

Investments as at 30 September 2021

Counterparty	Type	Amount £000	Rate %	Date of Investment	Date of Maturity
Goldman Sachs	Term	4,000	0.95%	30/07/2021	01/02/2022
Helaba	Term	4,000	0.95%	29/07/2021	29/10/2021
Plymouth City Council	Term	5,000	0.25%	09/09/2021	25/08/2022
Fixed Term Deposit sub total		**13,000**	**Listed in Order of Maturity**		
Debt Management Office	Term	17,000	0.01%	30-Sep-21	06-Oct-21
Debt Management Office sub total		**17,000**			
Santander UK PLC	180 Day Notice	6,000	0.40%	15/03/2016	n/a
Bank of Scotland	175 Day Notice	6,000	0.06%	30/11/2017	n/a
Notice Accounts sub total		**12,000**			
Barclays Fibca Deposit Account	Call	2,939	0.01%	**On Call**	
Call Accounts sub total		**2,939**			
Federated	MMF	5,000	0.01%	**On Call**	
Aberdeen Standard	MMF	5,000	0.01%	**On Call**	
Blackrock	MMF	5,000	0.01%	**On Call**	
Money Market Funds sub total		**15,000**			
Total		**59,939**			

Note:
(1) MMF rates are variable. This is the calculated average for the year to September.

Summary of Investments by Counterparty	Type	Amount £000	Limit £000
Aberdeen/Standard Life MMF	MMF	5,000	5,000
Bank of Scotland - 175 Day	175 Day Notice	6,000	6,000
Barclays	Call	2,939	6,000
BlackRock MMF	MMF	5,000	5,000
Debt Management Office	Term	17,000	Unlimited
Federated MMF	MMF	5,000	5,000
Goldman Sachs	Term	4,000	6,000
Helaba	Term	4,000	6,000
Plymouth City Council	Term	5,000	6,000
Santander UK - 180 Day	180 Day Notice	6,000	6,000
Total Investments		**59,939**	

APPENDIX B

APPENDIX C

Suggested Investment Durations as at 18 November 2021			
Country	**Counterparty**	**Suggested Duration**	**Limit per institution ***
United Kingdom	Bank of Scotland Plc	6 mths	£6m per group
	Lloyds Bank Plc	6 mths	
	Al Rayan Bank PLC	6 mths	£6m
	Barclays Bank PLC	6 mths	£6m
	Close Brothers Ltd	6 mths	£6m
	Clydesdale Bank PLC	100 days	£6m
	Coventry Building Society	6 mths	£6m
	Goldman Sachs International Bank	6 mths	£6m
	Handelsbanken PLC	12 mths	£6m
	HSBC Plc	12 mths	£6m
	Leeds Building Society	100 days	£6m
	Nationwide Building Society	6 mths	£6m
	National Westminster Bank	12 mths	£6m
	Nat West Markets PLC	100 days	£6m
	Royal Bank of Scotland	12 mths	£6m
	Santander UK Plc	6 mths	£6m
	Skipton Building Society	100 days	£6m
	Standard Chartered Bank	6 mths	£6m
	Sumitomo Mitsui Banking Corporation International Ltd	6 mths	£6m
	Yorkshire Building Society	100 days	£6m
Germany	Helaba (Landesbank Hessen-Thueringen Girozentrale)	12 mths	£4m

Notes:

Co-operative Bank, Nottingham BS, Principality BS, and West Bromwich BS had no suggested investment duration.

* Permitted by Council approval 24 February 2021.

APPENDIX D

Economics update

MPC meeting 24.9.21

- The Monetary Policy Committee (MPC) voted unanimously to leave the Bank Rate unchanged at 0.10% and made no changes to its programme of quantitative easing purchases due to finish by the end of this year at a total of £895bn; two MPC members voted to stop the last £35bn of purchases as they were concerned that this would add to inflationary pressures.

- There was a major shift in the tone of the MPC's minutes at this meeting from the previous meeting in August which had majored on indicating that some tightening in monetary policy was now on the horizon, but also not wanting to stifle economic recovery by too early an increase in Bank Rate. In his press conference after the August MPC meeting, Governor Andrew Bailey said, "the challenge of avoiding a steep rise in unemployment has been replaced by that of ensuring a flow of labour into jobs" and that "the Committee will be monitoring closely the incoming evidence regarding developments in the labour market, and particularly unemployment, wider measures of slack, and underlying wage pressures." In other words, it was flagging up a potential danger that labour shortages could push up wage growth by more than it expects and that, as a result, CPI inflation would stay above the 2% target for longer. It also discounted sharp increases in monthly inflation figures in the pipeline in late 2021 which were largely propelled by events a year ago e.g., the cut in VAT in August 2020 for the hospitality industry, and by temporary shortages which would eventually work their way out of the system: in other words, **the MPC had been prepared to look through a temporary spike in inflation.**

- So, in August the country was just put on alert. However, this time the MPC's words indicated there had been a marked increase in concern that more recent increases in prices, particularly the increases in gas and electricity prices in October and due again next April, are, indeed, likely to lead to **faster and higher inflation expectations and underlying wage growth, which would in turn increase the risk that price pressures would prove more persistent next year than previously expected. Indeed, to emphasise its concern about inflationary pressures, the MPC pointedly chose to reaffirm its commitment to the 2% inflation target in its statement;** this suggested that it was now willing to look through the flagging economic recovery during the summer to prioritise bringing inflation down next year. This is a reversal of its priorities in August and a long way from words at earlier MPC meetings which indicated a willingness to look through inflation overshooting the target for limited periods to ensure that inflation was 'sustainably over 2%'. Indeed, whereas in August the MPC's focus was on getting through a winter of temporarily high energy prices and supply shortages, believing that inflation would return to just under the 2% target after reaching a high around 4% in late 2021, now its primary concern is that underlying price pressures in the economy are likely to get embedded over the next year and elevate future inflation to stay significantly above its 2% target and for longer.

- Financial markets are now pricing in a first increase in Bank Rate from 0.10% to 0.25% in February 2022, but this looks ambitious as the MPC has stated that it wants to see what happens to the economy, and particularly to employment once furlough ends at the end of September. At the MPC's meeting in February it will only have available the employment figures for November: to get a clearer picture of employment trends, it would need to wait until the May meeting when it would have data up until February. At its May meeting, it will also have a clearer understanding of the likely peak of inflation.

APPENDIX D

- **The MPC's forward guidance on its intended monetary policy** on raising Bank Rate versus selling (quantitative easing) holdings of bonds is as follows: -
    1. Placing the focus on raising Bank Rate as "the active instrument in most circumstances".
    2. Raising Bank Rate to 0.50% before starting on reducing its holdings.
    3. Once Bank Rate is at 0.50% it would stop reinvesting maturing gilts.
    4. Once Bank Rate had risen to at least 1%, it would start selling its holdings.

- **COVID-19 vaccines.** These have been the game changer which have enormously boosted confidence that **life in the UK could largely return to normal during the summer** after a third wave of the virus threatened to overwhelm hospitals in the spring. With the household saving rate having been exceptionally high since the first lockdown in March 2020, there is plenty of pent-up demand and purchasing power stored up for services in hard hit sectors like restaurants, travel and hotels. The big question is whether mutations of the virus could develop which render current vaccines ineffective, as opposed to how quickly vaccines can be modified to deal with them and enhanced testing programmes be implemented to contain their spread.

US. See comments below on US treasury yields.

EU. The slow role out of vaccines initially delayed economic recovery in early 2021 but the vaccination rate has picked up sharply since then. After a contraction in GDP of -0.3% in Q1, Q2 came in with strong growth of 2%, which is likely to continue into Q3, though some countries more dependent on tourism may struggle. Recent sharp increases in gas and electricity prices have increased overall inflationary pressures but the ECB is likely to see these as being only transitory after an initial burst through to around 4%, so is unlikely to be raising rates for a considerable time.
German general election. With the CDU/CSU and SDP both having won around 24-26% of the vote in the September general election, the composition of Germany's next coalition government may not be agreed by the end of 2021. An SDP-led coalition would probably pursue a slightly less restrictive fiscal policy, but any change of direction from a CDU/CSU led coalition government is likely to be small. However, with Angela Merkel standing down as Chancellor as soon as a coalition is formed, there will be a hole in overall EU leadership which will be difficult to fill.

China. After a concerted effort to get on top of the virus outbreak in Q1 2020, economic recovery was strong in the rest of the year; this enabled China to recover all the initial contraction. During 2020, policy makers both quashed the virus and implemented a programme of monetary and fiscal support that was particularly effective at stimulating short-term growth. At the same time, China's economy benefited from the shift towards online spending by consumers in developed markets. These factors helped to explain its comparative outperformance compared to western economies during 2020 and earlier in 2021. However, the pace of economic growth has now fallen back after this initial surge of recovery from the pandemic and China is now struggling to contain the spread of the Delta variant through sharp local lockdowns - which will also depress economic growth. There are also questions as to how effective Chinese vaccines are proving. In addition, recent regulatory actions motivated by a political agenda to channel activities into officially approved directions, are also likely to reduce the dynamism and long-term growth of the Chinese economy.

APPENDIX D

Japan. 2021 has been a patchy year in combating Covid. However, after a slow start, nearly 50% of the population are now vaccinated and Covid case numbers are falling. After a weak Q3 there is likely to be a strong recovery in Q4. The Bank of Japan is continuing its very loose monetary policy but with little prospect of getting inflation back above 1% towards its target of 2%, any time soon: indeed, inflation was negative in July. New Prime Minister Kishida has promised a large fiscal stimulus package after the November general election – which his party is likely to win.

World growth. World growth was in recession in 2020 but recovered during 2021 until starting to lose momentum more recently. Inflation has been rising due to increases in gas and electricity prices, shipping costs and supply shortages, although these should subside during 2022. It is 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 from those in prior decades.

Supply shortages. The pandemic and extreme weather events have been highly disruptive of extended worldwide supply chains. At the current time there are major queues of ships unable to unload their goods at ports in New York, California and China. Such issues have led to mis-distribution of shipping containers around the world and have contributed to a huge increase in the cost of shipping. Combined with a shortage of semi-conductors, these issues have had a disruptive impact on production in many countries. Many western countries are also hitting up against a difficulty in filling job vacancies. It is expected that these issues will be gradually sorted out, but they are currently contributing to a spike upwards in inflation and shortages of materials and goods on shelves.

APPENDIX D

Interest rate forecasts

The Council's treasury advisor, Link Group, provided the following forecasts on 29th September 2021 (PWLB rates are certainty rates, gilt yields plus 80bps (0.8%):

Link Group Interest Rate View 29.9.21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.75
3 month ave earnings	0.10	0.10	0.20	0.20	0.30	0.40	0.50	0.50	0.60	0.70
6 month ave earnings	0.20	0.20	0.30	0.30	0.40	0.50	0.60	0.60	0.70	0.80
12 month ave earnings	0.30	0.40	0.50	0.50	0.50	0.60	0.70	0.80	0.90	1.00
5 yr PWLB	1.40	1.40	1.50	1.50	1.60	1.60	1.60	1.70	1.70	1.70
10 yr PWLB	1.80	1.80	1.90	1.90	2.00	2.00	2.00	2.10	2.10	2.10
25 yr PWLB	2.20	2.20	2.30	2.30	2.40	2.40	2.40	2.50	2.50	2.60
50 yr PWLB	2.00	2.00	2.10	2.20	2.20	2.20	2.20	2.30	2.30	2.40

Additional notes by Link on this forecast table: -

- *LIBOR and LIBID rates will cease from the end of 2021. Work is currently progressing to replace LIBOR with a rate based on SONIA (Sterling Overnight Index Average). In the meantime, our forecasts are based on expected average earnings by local authorities for 3 to 12 months.*
- *Our forecasts for average earnings are averages i.e., rates offered by individual banks may differ significantly from these averages, reflecting their different needs for borrowing short term cash at any one point in time.*

The coronavirus outbreak has done huge economic damage to the UK and to economies around the world. After the Bank of England took emergency action in March 2020 to cut Bank Rate to 0.10%, it left the Bank Rate unchanged at its subsequent meetings.

As shown in the forecast table above, one increase in the Bank Rate from 0.10% to 0.25% has now been included in quarter 2 of 2022/23, a second increase to 0.50% in quarter 2 of 23/24 and a third one to 0.75% in quarter 4 of 23/24.

Significant risks to the forecasts

- COVID vaccines do not work to combat new mutations and/or new vaccines take longer than anticipated to be developed for successful implementation.
- The pandemic causes major long-term scarring of the economy.
- The Government implements an austerity programme that supresses GDP growth.
- The MPC tightens monetary policy too early – by raising Bank Rate or unwinding QE.
- The MPC tightens monetary policy too late to ward off building inflationary pressures.
- Major stock markets e.g. in the US, become increasingly judged as being over-valued and susceptible to major price corrections. Central banks become increasingly exposed to the "moral hazard" risks of having to buy shares and corporate bonds to reduce the impact of major financial market sell-offs on the general economy.
- Geo-political risks are widespread e.g. German general election in September 2021 produces an unstable coalition or minority government and a void in high-profile

leadership in the EU when Angela Merkel steps down as Chancellor of Germany; on-going global power influence struggles between Russia/China/US.

The balance of risks to the UK economy: -

- The overall balance of risks to economic growth in the UK is now to the downside, including residual risks from Covid and its variants - both domestically and their potential effects worldwide.

Forecasts for Bank Rate

Bank Rate is not expected to go up fast after the initial rate rise as the supply potential of the economy has not generally taken a major hit during the pandemic, so should be able to cope well with meeting demand without causing inflation to remain elevated in the medium-term, or to inhibit inflation from falling back towards the MPC's 2% target after the surge to around 4% towards the end of 2021. Three increases in Bank rate are forecast in the period to March 2024, ending at 0.75%. However, these forecasts may well need changing within a relatively short time frame for the following reasons: -

- There are increasing grounds for viewing the economic recovery as running out of steam during the summer and now into the autumn. This could lead into stagflation which would create a dilemma for the MPC as to which way to face.
- Will some current key supply shortages e.g., petrol and diesel, spill over into causing economic activity in some sectors to take a significant hit?
- Rising gas and electricity prices in October and next April and increases in other prices caused by supply shortages and increases in taxation next April, are already going to deflate consumer spending power without the MPC having to take any action on Bank Rate to cool inflation. Then we have the Government's upcoming budget in October, which could also end up in reducing consumer spending power.
- On the other hand, consumers are sitting on around £200bn of excess savings left over from the pandemic so when will they spend this sum, in part or in total?

There are 1.6 million people coming off furlough at the end of September; how many of those will not have jobs on 1st October and will, therefore, be available to fill labour shortages in many sectors of the economy? So, supply shortages which have been driving up both wages and costs, could reduce significantly within the next six months or so and alleviate the MPC's current concerns.

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- There is a risk that there could be further nasty surprises on the Covid front, on top of the flu season this winter, which could depress economic activity.

In summary, with the high level of uncertainty prevailing on several different fronts, it is likely that these forecasts will need to be revised again soon - in line with what the new news is.

It also needs to be borne in mind that Bank Rate being cut to 0.10% was an emergency measure to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could decide to simply take away that final emergency cut from 0.25% to 0.10% on the grounds of it no longer being warranted and as a step forward in the return to normalisation. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.

Forecasts for PWLB rates and gilt and treasury yields
As the interest forecast table for PWLB certainty rates above shows, there is likely to be a steady rise over the forecast period, with some degree of uplift due to rising treasury yields in the US.

There is likely to be **exceptional volatility and unpredictability in respect of gilt yields and PWLB rates** due to the following factors: -

- How strongly will changes in gilt yields be correlated to changes in US treasury yields?
- Will the Fed take action to counter increasing treasury yields if they rise beyond a yet unspecified level?
- Would the MPC act to counter increasing gilt yields if they rise beyond a yet unspecified level?
- How strong will inflationary pressures turn out to be in both the US and the UK and so impact treasury and gilt yields?
- How will central banks implement their new average or sustainable level inflation monetary policies?
- How well will central banks manage the withdrawal of QE purchases of their national bonds i.e., without causing a panic reaction in financial markets as happened in the "taper tantrums" in the US in 2013?
- Will exceptional volatility be focused on the short or long-end of the yield curve, or both?

The forecasts are also predicated on an assumption that there is no break-up of the Eurozone or EU within our forecasting period, despite the major challenges that are looming up, and that there are no major ructions in international relations, especially between the US and China / North Korea and Iran, which have a major impact on international trade and world GDP growth.

Gilt and treasury yields

Since the start of 2021, there has been a lot of volatility in gilt yields, and hence PWLB rates. During the first part of the year, US President Biden's, and the Democratic party's determination to push through a $1.9trn (equivalent to 8.8% of GDP) fiscal boost for the US economy as a recovery package from the Covid pandemic was what unsettled financial markets. However, this was in addition to the $900bn support package already passed in December 2020 under President Trump. This was then followed by additional Democratic ambition to spend further huge sums on infrastructure and an American families plan over the next decade which are caught up in Democrat / Republican haggling. Financial markets were alarmed that all this stimulus, which is much bigger than in other western economies, was happening at a time in the US when: -

1. A fast vaccination programme has enabled a rapid opening up of the economy.
2. The economy had already been growing strongly during 2021.
3. It started from a position of little spare capacity due to less severe lockdown measures than in many other countries. A combination of shortage of labour and supply bottle necks is likely to stoke inflationary pressures more in the US than in other countries.
4. And the Fed was still providing monetary stimulus through monthly QE purchases.

These factors could cause an excess of demand in the economy which could then unleash stronger and more sustained inflationary pressures in the US than in other western countries. This could then force the Fed to take much earlier action to start tapering monthly QE purchases and/or increasing the Fed rate from near zero, despite their stated policy being to target average inflation. It is notable that some Fed members have moved forward their expectation of when the first increases in the Fed rate will occur in recent Fed meetings. In addition, more recently, shortages of workers appear to be stoking underlying wage inflationary pressures which are likely to feed through into CPI inflation. A run of strong monthly jobs growth figures could be enough to meet the threshold set by the Fed of "substantial further progress towards the goal of reaching full employment". However, the weak growth in August, (announced 3.9.21), has spiked anticipation that tapering of monthly QE purchases could start by the end of 2021. These purchases are currently acting as downward pressure on treasury yields. As the US financial markets are, by far, the biggest financial markets in the world, any trend upwards in the US will invariably impact and influence financial markets in other countries. However, during June and July, longer term yields fell sharply; even the large non-farm payroll increase in the first week of August seemed to cause the markets little concern, which is somewhat puzzling, particularly in the context of the concerns of many commentators that inflation may not be as transitory as the Fed is expecting it to be. Indeed, inflation pressures and erosion of surplus economic capacity look much stronger in the US than in the UK. **As an average since 2011, there has been a 75% correlation between movements in 10 year treasury yields and 10 year gilt yields. This is a significant UPWARD RISK exposure to our forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.**

There are also possible **DOWNSIDE RISKS** from the huge sums of cash that the UK populace have saved during the pandemic; when savings accounts earn little interest, it is likely that some of this cash mountain could end up being invested in bonds and so push up demand for bonds and support their prices i.e., this would help to keep their yields down. How this will interplay with the Bank of England eventually getting round to not reinvesting maturing gilts and then later selling gilts, will be interesting to keep an eye on.

The balance of risks to medium to long term PWLB rates: -

- There is a balance of upside risks to forecasts for medium to long term PWLB rates.

A new era – a fundamental shift in central bank monetary policy

One of the key results of the pandemic has been a fundamental rethinking and shift in monetary policy by major central banks like the Fed, the Bank of England and the ECB, to tolerate a higher level of inflation than in the previous two decades when inflation was the prime target to bear down on so as to stop it going <u>above</u> a target rate. There is now also a greater emphasis on other targets for monetary policy than just inflation, especially on 'achieving broad and inclusive "maximum" employment in its entirety' in the US before consideration would be given to increasing rates.

- The Fed in America has gone furthest in adopting a monetary policy based on a clear goal of allowing the inflation target to be symmetrical, (rather than a ceiling to keep under), so that inflation averages out the dips down and surges above the target rate, over an unspecified period of time.
- The Bank of England has also amended its target for monetary policy so that inflation should be 'sustainably over 2%' and the ECB now has a similar policy.
- <u>***For local authorities, this means that investment interest rates and very short term PWLB rates will not be rising as quickly or as high as in previous decades when the economy recovers from a downturn and the recovery eventually runs out of spare capacity to fuel continuing expansion.***</u>
- Labour market liberalisation since the 1970s has helped to break the wage-price spirals that fuelled high levels of inflation and has now set inflation on a lower path which makes this shift in monetary policy practicable. In addition, recent changes in flexible employment practices, the rise of the gig economy and technological changes, will all help to lower inflationary pressures.
- Governments will also be concerned to see interest rates stay lower as every rise in central rates will add to the cost of vastly expanded levels of national debt; (in the UK this is £21bn for each 1% rise in rates). On the other hand, higher levels of inflation will help to erode the real value of total public debt.

LINK ASSET SERVICES INTEREST RATE FORECASTS NOVEMBER 2021

	Bank Rate %			PWLB Borrowing Rates % (including 0.20% certainty rate adjustment)											
				5 year			10 year			25 year			50 year		
	Nov 21	Sep 21	Feb 21	Nov 21	Sep 21	Feb 21	Nov 21	Sep 21	Feb 21	Nov 21	Sep 21	Feb 21	Nov 21	Sep 21	Feb 21
Dec-21	0.25	0.10	0.10	1.50	1.40	0.90	1.80	1.80	1.30	2.10	2.20	1.90	1.90	2.00	1.70
Mar-22	0.25	0.10	0.10	1.50	1.40	1.00	1.90	1.80	1.40	2.20	2.20	2.00	2.00	2.00	1.80
Jun-22	0.50	0.25	0.10	1.60	1.50	1.00	1.90	1.90	1.40	2.30	2.30	2.00	2.10	2.10	1.80
Sep-22	0.50	0.25	0.10	1.60	1.50	1.10	2.00	1.90	1.50	2.40	2.30	2.10	2.20	2.20	1.90
Dec-22	0.50	0.25	0.10	1.70	1.60	1.10	2.00	2.00	1.50	2.40	2.40	2.10	2.20	2.20	1.90
Mar-23	0.75	0.25	0.10	1.70	1.60	1.10	2.10	2.00	1.50	2.40	2.40	2.10	2.20	2.20	1.90
Jun-23	0.75	0.50	0.10	1.70	1.60	1.20	2.10	2.00	1.60	2.50	2.40	2.20	2.30	2.20	2.00
Sep-23	0.75	0.50	0.10	1.80	1.70	1.20	2.20	2.10	1.60	2.50	2.50	2.20	2.30	2.30	2.00
Dec-23	0.75	0.50	0.10	1.80	1.70	1.20	2.20	2.10	1.60	2.60	2.50	2.20	2.40	2.30	2.00
Mar-24	1.00	0.75	0.10	1.80	1.70	1.20	2.20	2.10	1.60	2.60	2.50	2.20	2.40	2.40	2.00
Jun-24	1.00			1.90			2.30			2.60			2.40		
Sep-24	1.00			1.90			2.30			2.60			2.40		
Dec-24	1.00			2.00			2.30			2.70			2.50		
Mar-25	1.25			2.00			2.40			2.70			2.50		

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