Annual Treasury Management Review

2019/20

English Local Authorities

April 2020

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1. Introduction

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2019/20. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management, (the Code), and the CIPFA Prudential Code for Capital Finance in Local Authorities, (the Prudential Code).

During 2019/20 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 07/02/2019)
- a mid-year (minimum) treasury update report (Cabinet 18/12/2019)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

In addition, Cabinet and the Finance, Audit and Risk (FAR) Committee have received quarterly treasury management update reports.

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Finance Audit and Risk Committee before they were reported to the full Council.

2. The Council's Capital Expenditure and Financing

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- 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 need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

	2018/19 Actual £'000	2019/20 Working Budget £'000	2019/20 Actual £'000
Capital expenditure	**5,574**	**1,804**	**1,473**
Financed in year	1,233	1,220	1,076
Unfinanced capital expenditure	**4,341**	**584**	**397**

3. The Council's Overall Borrowing Need

The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2019/20 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies, (such as the Government, through the Public Works Loan Board [PWLB], or the money markets), or utilising temporary cash resources within the Council.

CFR (£m): General Fund	31 March 2019 Actual	31 March 2020 Budget	31 March 2020 Actual
Opening balance	-10,335	-4,394	-5,993
Add unfinanced capital expenditure (as above)	4,342	4,332	397
Closing balance	-5,993	-62	**-5,596**

Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2019/20) plus the estimates of any additional capital financing requirement for the current (2020/21) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2019/20. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	31 March 2019 Actual £'000	31 March 2020 Budget £'000	31 March 2020 Actual £'000
Gross borrowing position	440	423	423
CFR	-5,993	-62	-5,596

The CFR is negative as the Council has more cash investments than borrowing. Borrowing is historic and was undertaken prior to the housing stock transfer when the CFR was positive.

The authorised limit - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2019/20 the Council has maintained gross borrowing within its authorised limit.

The operational boundary – the operational boundary 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.

Actual financing costs as a proportion of net revenue stream - - this indicator is the net cost of borrowing as a percentage of the total revenue budget. This would usually show how much of the overall budget is spent on borrowing costs. However as the Councils investment income exceeds the cost of interest on borrowing it is a negative number.

	2019/20
Authorised limit	£10.0m
Maximum gross borrowing position during the year	£0.440m
Operational boundary	£4.1m
Average gross borrowing position	£0.432m
Financing costs as a proportion of net revenue stream	-2.3%

4. Treasury Position as at 31 March 2020

At the end of 2019/20 the Council's treasury position was as follows:

	31 March 2019 Principal £'000	Rate/ Return	31 March 2020 Principal £'000	Rate/ Return
Fixed rate borrowing:				
-PWLB	440	9.7%	423	9.82%
-Market	0		0	
Variable rate borrowing:				

-PWLB	0		0	
-Market	0		0	
Total debt	**440**	**9.7%**	**423**	**9.82%**
CFR	**-5,993**		**-5,596**	
Over / (under) borrowing	**6,433**		**6,019**	
Investments:				
Total investments	**30,000**	**1.17%**	**29,500**	**1.18%**

The maturity structure of the debt portfolio was as follows:

	31 March 2019 Actual £'000	31 March 2020 Actual £'000
Under 12 months	17	18
12 months and within 24 months	18	18
24 months and within 5 years	58	61
5 years and within 10 years	82	69
10 years and above	265	257

The table below summaries where investments were held at 31 March and includes the Lloyds Bank interest bearing current account:

INVESTMENT PORTFOLIO	Actual 31.3.19 £000	Actual 31.3.19 %	Actual 31.3.20 £000	Actual 31.3.20 %
Treasury investments				
Banks	9,900	30	10,000	27
Building Societies	16,500	51	9,500	25
Local authorities	6,000	19	16,000	43

Money Market Funds	0	0	0	0
Central Government	0	0	2,000	5
TOTAL TREASURY INVESTMENTS	32,400	100	37,500	100

Money market funds provide a short-term investment option with no entry or exit fees. Due to changes in accounting regulations the Council would have been required to obtain (and possibly pay for) professional advice on the risk of default in relation to balances held in Money Market Funds at 31st March 2020. To avoid these fees, it was decided to temporarily remove the funds and then reinvest them after the 1st April 2020.

The maturity structure of the investment portfolio was as follows:

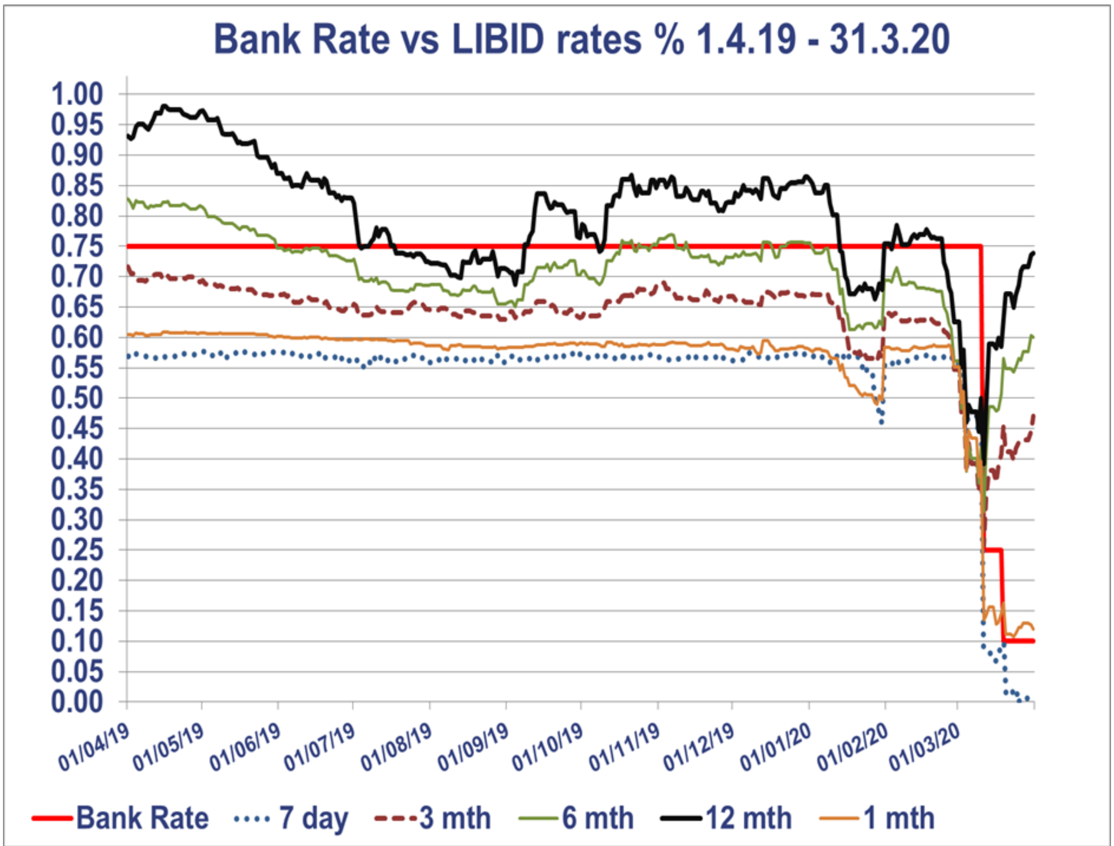
	2018/19 Actual £000	31 March 2020 Actual £000
Investments Longer than 1 Year	1,500	1,000
Investments Up to1 Year	28,500	28,500
Total	30,000	29,500

5. The strategy for 2019/20

The strategy in 2019/20 was to continue only lending to UK banks, building societies, money market funds, Local Authorities and property funds. Only UK banks with a credit rating, for longer term deals, greater than “BBB” and F3 or above for short term credit ratings were on the Council’s lending list. (These are Fitch definitions of ratings). Not all building societies are credit rated but this did not preclude them from the lending list as lending to a building society was dependant on their asset size. Where a society did have a rating, this was considered at the time of the deal taking into account the amount of investment and the length of the deal. In addition, the strategy was changed in 2019/20 to allow investments with non-UK banks with a credit rating greater than AA- with a AAA Country rating. The strategy moved from imposing limits based on a percentage of the total investments outstanding to a fixed limit.

Change in strategy during the year – the strategy adopted in the original Treasury Management Strategy Report for 2019/20, approved by the Council on 07/02/2019, was not changed during the year.

5.1 Investment strategy and control of interest rate risk



	Bank Rate	7 day	1 mth	3 mth	6 mth	12 mth
High	0.75	0.58	0.61	0.72	0.83	0.98
High Date	01/04/2019	09/05/2019	15/04/2019	01/04/2019	01/04/2019	15/04/2019
Low	0.10	0.00	0.11	0.26	0.31	0.39
Low Date	19/03/2020	25/03/2020	23/03/2020	11/03/2020	11/03/2020	11/03/2020
Average	0.72	0.53	0.56	0.63	0.70	0.80
Spread	0.65	0.58	0.50	0.46	0.52	0.59

Link Asset Services Interest Rate View	31.3.20							
	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 Month LIBID	0.45	0.40	0.35	0.30	0.30	0.30	0.30	0.30
6 Month LIBID	0.60	0.55	0.50	0.45	0.40	0.40	0.40	0.40
12 Month LIBID	0.75	0.70	0.65	0.60	0.55	0.55	0.55	0.55
5yr PWLB Rate	1.90	1.90	1.90	2.00	2.00	2.00	2.10	2.10
10yr PWLB Rate	2.10	2.10	2.10	2.20	2.20	2.20	2.30	2.30
25yr PWLB Rate	2.50	2.50	2.50	2.60	2.60	2.60	2.70	2.70
50yr PWLB Rate	2.30	2.30	2.30	2.40	2.40	2.40	2.50	2.50

Investment returns remained low during 2019/20. The expectation for interest rates within the treasury management strategy for 2019/20 was that Bank Rate would stay at 0.75% during 2019/20 as it was not expected that the MPC would be able to deliver on an increase in Bank Rate until the Brexit issue was finally settled. However, there was an expectation that Bank Rate would rise after that issue was settled, but would only rise to 1.0% during 2020.

Rising concerns over the possibility that the UK could leave the EU at the end of October 2019 caused longer term investment rates to be on a falling trend for most of April to September. They then rose after the end of October deadline was rejected by the Commons but fell back again in January before recovering again after the 31 January departure of the UK from the EU. When the coronavirus outbreak hit the UK in February/March, rates initially plunged but then rose sharply back up again due to a shortage of liquidity in financial markets. As longer term rates were significantly higher than shorter term rates during the year, value was therefore sought by placing longer term investments where cash balances were sufficient to allow this.

6. Borrowing Outturn

Borrowing

No new long term loans were taken during the year.

A temporary loan of £2.0M was borrowed for cash flow on the 20 June until the 1 July at a rate of 0.7%

£17K of PWLB loans were repaid during the year, as they became due.

Borrowing in advance of need

The Council has not borrowed more than, or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed.

Rescheduling

No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

7. Investment Outturn

Investment Policy – the Council's investment policy is governed by MHCLG investment guidance, which has been implemented in the annual investment strategy approved by the Council on 07/02/19. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the Fitch credit rating agency for banks and asset size for building societies.

The investment activity during the year conformed to the approved strategy. The £5M limit on the Council's current account was exceeded on two separate occasions and were reported to Members in the quarterly monitoring reports.

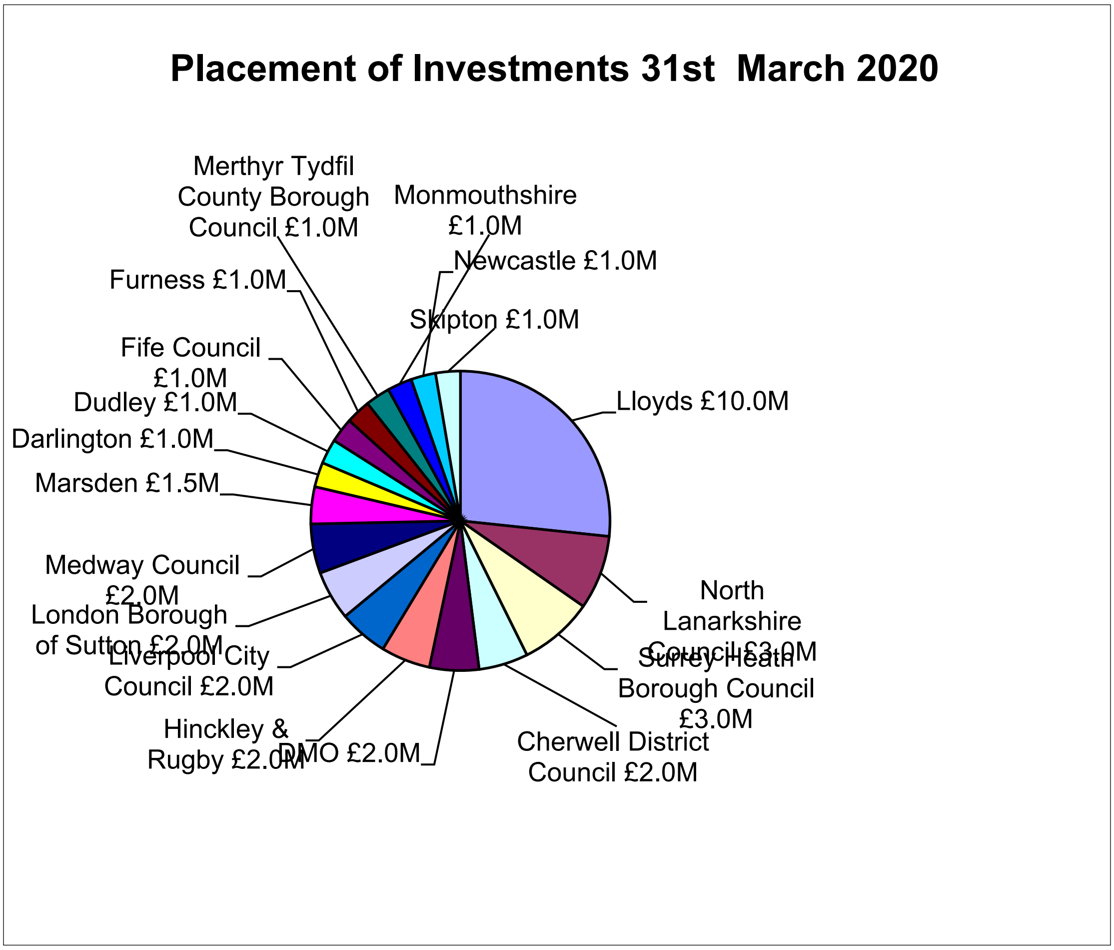
Investments placed by Cash Managers – the Council used an external cash manager to invest some of its longer term cash balances, where the rate achieved (after fees) is better than can be obtained by the Council directly. At the start of the year, Tradition had £8.5m of outstanding investments. This remained the same throughout the year. The performance of the Tradition against the benchmark return was:

Cash Manager	Investments Placed	Interest	Return	Benchmark*
Tradition	£8.5M	£0.116M	1.36%	0.55%

* Ave 7 days notice Rate 0.55%

This compares with an original budget of £0.111M.

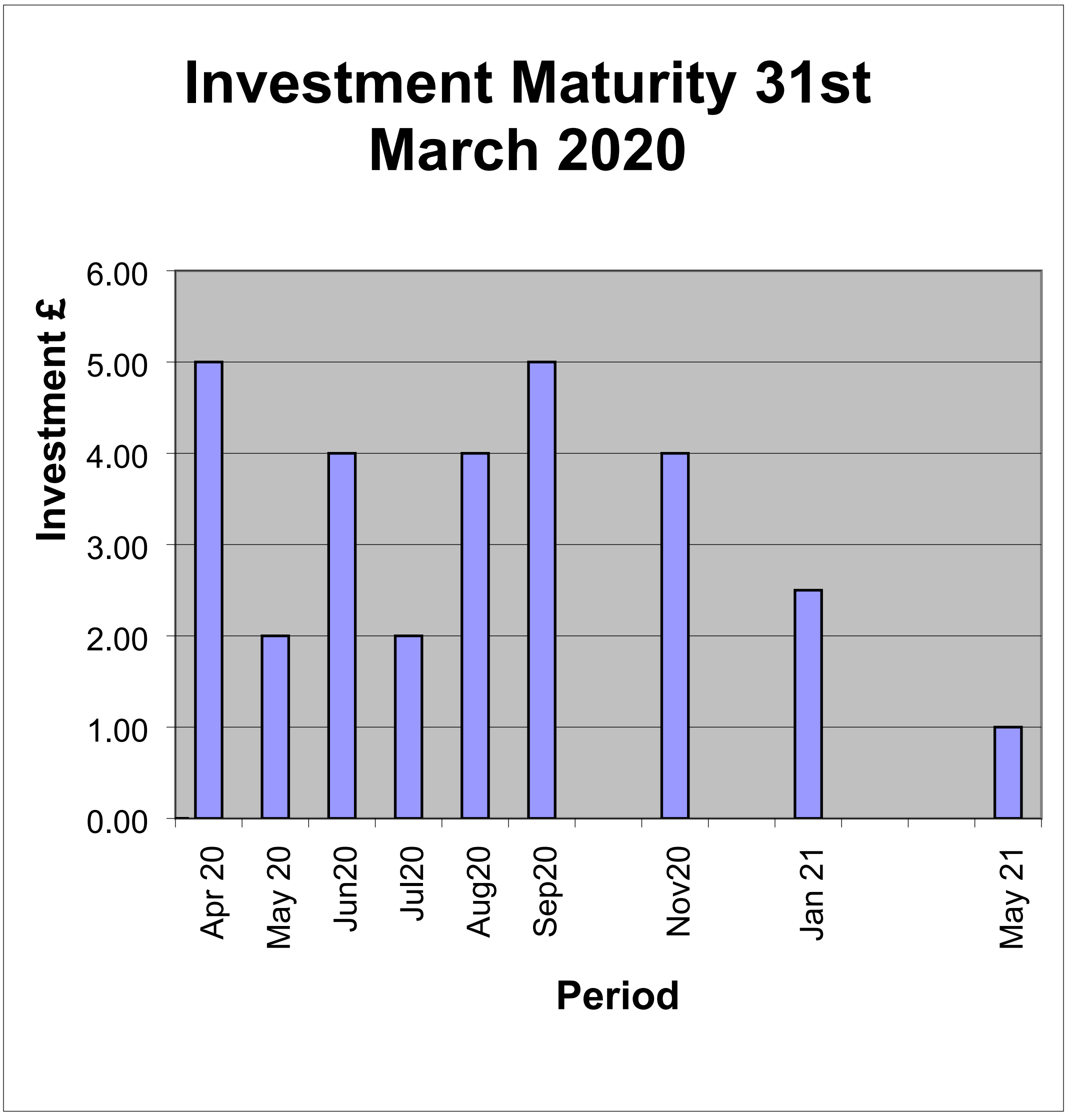
The pie chart below shows the spread of investment balances as at 31 March 2020. This is a snapshot in time that demonstrates the diversification of investments.



The average daily balance of investments was £39.8m with balances varying between £29.5m and £51.0m.

£0.411m of interest was generated from investments during the year. This is slightly less than the estimated interest of £0.418m (as per Quarter 3 forecast).

The graph below shows the maturity profile of investments at 31st March 2020.



The level of risk of any investment will be affected by the riskiness of the institution where it is invested and the period that it is invested for. Where an institution has a credit rating this can be used to measure its riskiness. This can be combined with the period remaining on the investment to give a historic risk of default percentage measure. The table below shows the Historic Risk of Default for outstanding investments at 31 March. The most risky investment still has a historic risk of default of below 1%. It should also be noted that in general the interest rate received is correlated to the risk, so the interest income received would be less if it took on less risk. All investments have been made in accordance with the Investment Strategy.

Borrower	Interest Rate %	Principal	Days to Maturity from 31/03/20	Historic Risk of Default	Risk of Default
DMO	0.09	2,000,000	3	0.00%	0.00000
HINCKLEY & RUGBY	1.35	2,000,000	24	0.15%	0.00010
SKIPTON	0.92	1,000,000	29	0.15%	0.00012
DUDLEY	1.3	1,000,000	37	0.15%	0.00015
MERTHYR TYDFIL COUNTY BOROUGH COUNCIL	0.85	1,000,000	58	0.00%	0.00000
FURNESS	1.3	1,000,000	63	0.15%	0.00026
LONDON BOROUGH OF SUTTON	0.8	2,000,000	66	0.00%	0.00000
FIFE COUNCIL	1.15	1,000,000	90	0.00%	0.00000
LIVERPOOL CITY COUNCIL	0.83	2,000,000	118	0.00%	0.00000
LLOYDS	1.25	1,000,000	125	0.05%	0.00017
SURREY HEATH BOROUGH COUNCIL	0.9	3,000,000	146	0.00%	0.00000
NORTH LANARKSHIRE COUNCIL	0.9	3,000,000	163	0.00%	0.00000
CHERWELL DISTRICT COUNCIL	0.87	2,000,000	174	0.00%	0.00000
LLOYDS	1.1	1,000,000	219	0.05%	0.00030
MEDWAY COUNCIL	1.25	2,000,000	220	0.00%	0.00000
NEWCASTLE	1.17	1,000,000	241	0.15%	0.00099
DARLINGTON	1.2	1,000,000	283	0.15%	0.00116
MARSDEN	1.6	1,500,000	297	0.15%	0.00122
MONMOUTHSHIRE	1.5	1,000,000	423	0.15%	0.00174

Resources – the Council’s cash balances comprise revenue and capital resources and cash flow monies. The Council’s core cash resources comprised as follows:

Balance Sheet Resources	31 March 2019 £,000	31 March 2020 £’000
Balances	**8,800**	**9,332**
Earmarked reserves	**7,184**	**9,271**
Provisions	**1,245**	**2,446**
Usable capital receipts	**2,580**	**1,941**
Total	**19,679**	**22,990**