Waveney District Council

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AUDIT & GOVERNANCE COMMITTEE

Wednesday, 25 July 2018

TREASURY MANAGEMENT OUTTURN REPORT FOR 2017/18 & MID YEAR REPORT FOR 2018/19 (REP1842)

EXECUTIVE SUMMARY

1. The Treasury Management Policy Statement for 2017/18 requires an annual report and mid year report to be produced by the 30th September 2018 and approved at Full Council.
2. The report reviews performance of the treasury management function including prudential indicators in 2017/18 and incorporates a mid year review of 2018/19.

2017/18 Summary:

- Investments totalled £41.50m as at 31st March 2018.
- Interest received during the year totalled £260k.
- The Council maintained its policy of investing short term rather than longer term (greater than one year) due to market conditions.
- The Council operated within its approved Prudential Indicator Limits for 2017/18.

2018/19 Summary to date:

- Investments totalled £44.7m as at 30th June 2018.
- Interest received to 30th June 2018 totalled £51k.
- The Council has operated within its approved Prudential Indicator Limits to date.

Is the report Open or Exempt?	Open

Wards Affected:	All Wards within the District

Cabinet Member:	Councillor Bruce Provan Cabinet Member for Resources

Supporting Officer:	Homira Javadi Chief Finance Officer (01394) 444529 homira.javadi@eastsuffolk.gov.uk

1 INTRODUCTION

1.1 Treasury Management in Local Government is governed by the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management in the Public Services and in this context is the "management of the Council's cash flows, its banking and its capital market transactions; the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks". This Council has adopted the Code and complies with its requirements.

1.2 The Council approves a strategy report at the beginning of each financial year, which identifies how it proposes to borrow and invest in the light of capital spending requirements, interest rate forecasts and economic conditions. The Cabinet monitors the implementation of the treasury strategy and reports are received quarterly during the year. The Audit & Governance Committee are responsible for ensuring scrutiny of the treasury management activities.

1.3 Under the Prudential Code for Capital Finance in Local Authorities, the Council determines at a local level its capital expenditure and can borrow or use alternative financing methods to finance capital spending provided that capital plans are demonstrably affordable, prudent and sustainable. The Code requires prudential indicators to be set and monitored, some of which are limits.

1.4 By the end of September each year, councils must report on their treasury management activities that have taken place over the year to Full Council. The remainder of this report summarises the year's activities and performance and provides an update on the activities that have taken place during the first half of the next financial year.

TREASURY MANAGEMENT OUTTURN 2017/18

2 THE ECONOMY AND INTEREST RATES

2.1 2017-18 was characterised by the push-pull from expectations of tapering of Quantitative Easing (QE) and the potential for increased policy rates in the US and Europe and from geopolitical tensions, which also had an impact.

2.2 The UK economy showed signs of slowing with latest estimates showing Gross Domestic Product (GDP), helped by an improving global economy, grew by 1.8% in calendar 2017, the same level as in 2016. This was a far better outcome than the majority of forecasts following the European Union (EU) Referendum in June 2016, but it also reflected the international growth momentum generated by the increasingly buoyant United States (US) economy and the re-emergence of the Eurozone economies.

2.3 The Bank of England's Monetary Policy Committee (MPC) increased Bank Rate by 0.25% in November 2017. It was significant in that it was the first rate hike in ten years, although in essence the MPC reversed its August 2016 cut following the referendum result. The February Inflation Report indicated the MPC was keen to return inflation to the 2% target over a more conventional (18-24 month) horizon with 'gradual' and 'limited' policy tightening. Although in March two MPC members voted to increase policy rates immediately and the MPC itself stopped short of committing itself to the timing of the next increase in rates, the minutes of the meeting suggested that an increase in May 2018 was highly likely, but this did not materialise.

3 BORROWING

3.1 During 2017/18 the Council did not enter in to any new borrowing arrangements.

3.2 Given the large differential between short and longer term interest rates, which is likely to remain a feature for some time, as well as the pressure on Council finances, the debt management strategy sought to lower debt costs within an acceptable level of volatility (interest rate risk). Loans that offered the best value in the prevailing interest rate environment were PWLB variable interest rates loans. This supported the case for maintaining the Council's variable rate debt portfolio.

3.3 Given the significant cuts to local government funding putting pressure on Council finances, the strategy followed was to minimise debt interest payments without compromising the longer-term stability of the portfolio. The use of internal resources in lieu of borrowing was judged to be the most cost effective means. The 2017/18 borrowing requirement for the General Fund capital programme was £1.46m for which cash balances were utilised. If the Council would have sought to borrow this amount on a short term one year basis this would have attracted an interest cost of approximately £22.92k at a rate of 1.57%. The average interest amount lost by not having this amount invested would have been approximately £10.51k at 0.72%, therefore making a saving of £12.41k.

3.4 The current debt portfolio of the Council can be seen in the table below and is summarised by £75.98m attributable to the HRA which includes £68.3m of Self-Financing loans taken out in 2011/12 and £11.76m of General Fund loans.

Loans as at 31/3/2018	**Principal £m**	**Rate Range %**	**Maturity Range (years)**
PWLB Fixed Rate Maturity Loans	67.45	3.01 - 8.38	4.0- 42.0
PWLB Variable Rate Maturity Loans	20.29	0.42 – 0.43	1.0 – 4.0
Total	**87.74**	**0.42 - 8.38**	**1.0 - 42.0**

4 INVESTMENT ACTIVITY

4.1 The Councils investment policy for 2017/18 was governed by Department of Communities and Local Government (DCLG) guidance and implemented in the annual investment strategy approved by the Council on 25th January 2017. This policy set out the approach for choosing investment counterparties and was based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.). The DCLG's Investment Guidance requires local authorities to focus on security and liquidity, rather than yield.

4.2 The Council held an average cash balance of £43.19m during the year and received investment income of £260k which exceeded its original planned budget of £180k for 2017/18.

	Balance at 1st April 2017	Investment made	Investments repaid	Balance at 31st March 2018
INVESTMENTS	£m	£m	£m	£m
Short Term Investments (liquidity & term <12 months)	39.00	86.50	-84.00	41.50

4.3 As at the 31st March 2018 the investment profile of the Council was as follows.

INVESTMENTS	Balance at 31st March 2018 £m
Liquidity Investments	5.0
Short Term investments	
April 2017 to April 2018	3.00
May 2017 to May 2018	2.00
June 2017 to June 2018	5.00
July 2017 to July 2018	2.00
August 2017 to August 2018	2.00
September 2017 to September 2018	2.00
October 2017 to April 2018	2.00
November 2017 to May 2018	2.00
February 2018 to May 2018	3.00
February 2018 to June 2018	3.00
March 2018 to April 2018	8.00
Long Term investments	
November 2017 - onwards	2.50
Total	41.50

4.4 Security of capital remained the Council's main investment objective. This was maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2017/18.

4.5 Investments during the year included call accounts and deposits with Banks and Building Societies within the UK. During the year there were no investments placed with counterparties outside of the UK.

4.6 There were no changes to the Councils list of approved investment institutions (counterparty list) during the year.

4.7 All investments made during the year complied with the Council's agreed Treasury Management Strategy, Prudential Indicators, and Treasury Management Practices and prescribed limits. Maturing investments were repaid to the Council in full and in a timely manner.

4.8 Counterparty credit quality was assessed and monitored with reference to credit ratings; credit default swaps; GDP of the country in which the institution operates; the country's net debt as a percentage of GDP; any potential support mechanisms and share price. The minimum long-term counterparty credit rating determined for the 2017/18 treasury strategy was F1 Short term and A- Long term across rating agencies Fitch, Standard & Poor's and Moody's.

4.9 The Council sought to optimise returns commensurate with its objectives of security and liquidity. The Bank of England Base Rate was increased from 0.25% to 0.50% on 2nd November 2017.

5 COMPLIANCE WITH PRUDENTIAL INDICATORS

5.1 The Council complied with its Prudential Indicators for 2017/18, which was approved on 25th January 2017. The Prudential Indicators for 2017/18 can be found in Appendix A.

6 TREASURY MANAGEMENT STRATEGY AND ANNUAL INVESTMENT STRATEGY UPDATE

6.1 The Treasury Management Strategy Statement (TMSS) for 2018/19 was approved at Council on 24th January 2018 and there have been no policy changes to date.

7 DAILY CASH MANAGMENT

7.1 The Council's counterparty list (investment list) is continuously reviewed and updated taking into account published credit rating information, financial accounts, share prices, asset size, Government support and information from the Council's Treasury Advisors, Arlingclose.

8 INVESTMENT PORTFOLIO 2018/19

8.1 The Council held £44.7m of investments as at the 30th June 2018; the table below illustrates the maturity of investments over the forthcoming months and the average interest rate achieved on the investment.

	1st April 2018 £m	Average Interest Rate %	30th June 2018 £m	Average Interest Rate %
Call Accounts (Liquidity Funds)	5.0	0.40	16.31	0.32
Term Investments: 3 to 12 months	36.5	0.77	26.0	0.57
Property Investment Fund	2.39	4.69	2.39	4.69

8.2 The Council can confirm that the approved limits within the Annual Investment Strategy were not breached during the first three months of 2018/19.

9 ECONOMIC OUTLOOK

9.1 The May inflation report showed the Bank of England amended its growth forecast for the UK to reach 1.9% in 2017. Inflation forecasts are now expected to remain above the 2% target until 2020.

9.2 The headline inflation figure, CPIT, rose to 2.9% in May on an annual basis, whilst the monthly figure was recorded at 0.3%. The weaker pound is seen as a key contributor to this rise.

9.3 The second estimate for UK Quarter One Gross Domestic Product (GDP) showed quarterly growth slowed to 0.2% quarter on quarter. Growth rose by 2.0% year on year, an increase from 1.0% previously recorded in Quarter Four 2016. Both figures were downward revisions from the previous estimates of 0.3% quarter on quarter and 2.1% year on year.

10 BASE RATE FORECAST

10.1 The Treasury Management Strategy and Investment Strategy 2018/19 included the following forecast on the Bank of England Base Rate, with the anticipation that the rate would increase over the coming year.

	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19
Upside Risk	0.00%	0.00%	0.00%	0.00%	0.00%	0.25%	0.25%
Base Rate	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.25%
Downside Risk	0.00%	-0.25%	-0.25%	-0.50%	-0.50%	-0.75%	-0.75%

10.2 Although there have been some talk of a rate rise, and the widely predicted rise in May 2018 did not materialise the likely outcome is that rates will continue at their current level for another year.

11 TREASURY MANAGEMENT PRACTICES (TMPS)

11.1 As a backdrop to the Council's approved treasury management policies, the Council also maintains a number of Treasury Management Practices (TMPS) which set out the manner in which the Council seeks to achieve the policies and objectives of the treasury function and how it will manage and control those activities. These were approved at Council on 30th September 2013.

11.2 There have been no major changes during 2017/18 and during the first half of 2018/19.

11.3 The TMPS can be viewed within the Finance service area on the Council's intranet page or by contacting the Financial Services Compliance Team.

12 INVESTMENT POLICY UPDATE

12.1 The Council's investment policy has regard to the DCLG's Guidance on Local Government Investments, Investment Regulations and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes. The Council's investment priorities will be security first, liquidity second, and then return.

13 CREDITWORTHINESS POLICY UPDATE

13.1 The Chief Finance Officer will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary.

13.2 Credit rating information is supplied by Arlingclose, our treasury consultants, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating Watches (notification of a likely change), rating Outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing.

Banks 1 - good credit quality – the Council will only use banks which:

i. are UK banks; and/or

ii. are non-UK and domiciled in a country which has a minimum sovereign long term rating of AA+

and have, as a minimum, the following Fitch, Moody's and Standard and Poor's credit ratings (where rated):

i. Short term – F1

ii. Long term – A-

13.3 Viability, Financial Strength and Support ratings have been removed and will not be considered in choosing counterparties. All other criteria remains as previously approved.

14 BANKING ARRANGEMENTS

14.1 Banking services for the Council are provided by Lloyds Banks Plc.

15 TREASURY MANAGEMENT ADVISORS

15.1 The external treasury advisors for the Council is Arlingclose

16 HOW DOES THIS RELATE TO EAST SUFFOLK BUSINESS PLAN?

16.1 The Treasury Management Outturn and Mid Year report is a CIPFA requirement, the report does not link directly to the Vision of the Business Plan, but through ensuring good governance arrangements and security of the Councils investment income this will help to achieve the planned actions set out in the Business Plan.

17 FINANCIAL AND GOVERNANCE IMPLICATIONS

17.1 This report is to provide an update of the treasury management governance arrangements and performance for the previous and current year.

18 CONSULTATION

18.1 There is no requirement upon the Council.

19 OTHER OPTIONS CONSIDERED

19.1 No other options were considered.

20 REASON FOR RECOMMENDATION

20.1 The CIPFA Treasury Management Code requires a report to be produced covering the Council's Treasury Management activities during 2017/18 and a Mid Year Review of the Treasury Management activities that have taken place during the first half of 2018/19. These reports must be approved by 30th September 2018.

RECOMMENDATIONS

1. That the Annual Report on the Council's Treasury Management activity for 2017/18 incorporating the Mid Year review for 2018/19 be recommended to Full Council for approval at its September meeting.
2. That the Prudential Indicators Outturn position for 2017/18 in Appendix A be noted.

APPENDICES	
Appendix A	Prudential Indicators Outturn for 2017/18

BACKGROUND - none

APPENDIX A

Compliance with Prudential Indicators 2017/18

1 ESTIMATED AND ACTUAL CAPITAL EXPENDITURE

1.1 This indicator is set to ensure that the level of proposed investment in capital assets remains within sustainable limits and in particular, to consider the impact on the Council Tax and in the case of the HRA, housing rent levels.

	2017/18	**2017/18**
	Estimated £m	**Outturn £m**
Capital Expenditure		
Non-HRA	7.19	**2.03**
HRA	10.99	**7.00**
Total Capital Expenditure	**18.18**	**9.03**

1.2 The £5.16m variance on Non-HRA relates to programme delivery being deferred until 2018/19 with £4.04m directly attributable to the Tidal /barrier scheme. The £3.99m variance on HRA relates to programme delivery being deferred until 2017/18 mainly due to with £0.70m directly attributable to the Housing development scheme**.**

2 ESTIMATED AND ACTUAL RATIO OF FINANCING COSTS TO NET REVENUE STREAM

2.1 This is an indicator of affordability and demonstrates the revenue implications of capital investment decisions by highlighting the proportion of the revenue budget required to meet the borrowing costs associated with capital spending. The financing costs include existing and proposed capital commitments. Any increase in the percentages requires an increased contribution from the revenue account to meet the borrowing cost. The HRA variance is due to a reduced capital outturn position compared to what had been budgeted.

	2017/18	2017/18
	Estimated %	Outturn %
Ratio of Financing Costs to Net Revenue Stream		
Non-HRA	15.28	12.72
HRA	34.40	28.17

3 CAPITAL FINANCING REQUIREMENT

3.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. In order to ensure that over the medium term net borrowing will only be for a capital purpose, the Council ensures that net external borrowing does not, except in the short term, exceed the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years.

3.2 The Council met this requirement in 2017/18.

	2017/18	2017/18
	Estimated £m	Outturn £m
Capital Financing Requirement		
Non-HRA	30.85	29.98
HRA	77.75	77.75
Total	**108.60**	**107.83**

4 AFFORDABLE BORROWING LIMIT, AUTHORISED LIMIT AND OPERATIONAL BOUNDARY FOR EXTERNAL DEBT

4.1 **Authorised Limit**: This is the maximum amount of external debt that can be outstanding at one time during the financial year. The limit, which is expressed gross of investments, is consistent with the Council's existing commitments, proposals for capital expenditure and financing and with its approved treasury policy and strategy and also provides headroom over and above for unusual cash movements. This limit was set at £122m for 2017/18, with the actual total borrowing being £87.73m.

4.2 **Operational Boundary**: This limit is set to reflect the Council's best view of the most likely prudent (i.e. not worst case) levels of borrowing activity and was set at £119m for 2016/17 with the actual borrowing amount being £87.73.

4.3 The levels of debt are measured on an ongoing basis during the year for compliance with the Authorised Limit and the Operational Boundary. The Council maintained its total external borrowing and other long-term liabilities within both limits.

5 UPPER LIMITS FOR FIXED INTEREST RATE EXPOSURE AND VARIABLE INTEREST RATE EXPOSURE

5.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The exposures are calculated on a net basis, i.e. fixed rate debt net of fixed rate investments. The upper limit for variable rate exposure allows for the use of variable rate debt to offset exposure to changes in short-term rates on our portfolio of investments.

	2017/18	2017/18
	Estimated %	Outturn %
Upper Limit for Fixed Rate Exposure	100	77
Upper Limit for Variable Rate Exposure	50	23

6 MATURITY STRUCTURE OF FIXED RATE BORROWING

6.1 This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

6.2 It is calculated as the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate.

Maturity structure of fixed rate borrowing	Upper limit %	Lower limit %	Actual Borrowing as at 31/03/2018 £m	Percentage of total as at 31/03/2018 %
under 12 months	50	0	0	0
1 year and within 2 years	50	0	0	0
2 years and within 5 years	75	0	1.0	1
5 years and within 10 years	75	0	12.0	18
10 years and within 20 years	75	0	13.76	20
20 years and above	100	0	41.00	61

6.3 All borrowing has been taken in conjunction with advice from the Council's Treasury Management Advisors.

7 TOTAL PRINCIPAL SUMS INVESTED FOR PERIODS LONGER THAN 364 DAYS

7.1 There were no proposals for the Council to invest sums for periods longer than 364 days.