REPORT TO	ON
Governance Committee	24 September 2019

External Audit Annual

TITLE	REPORT OF
Treasury Management Annual Report 2018/19 and June Quarter Monitoring 2019/20	Interim S151 Officer

Is this report confidential?	**No**

1. PURPOSE OF THE REPORT

1.1 To present the outturn for Treasury Management activity in financial year 2018/19.
1.2 To present monitoring information for the quarter to June 2019.

2. RECOMMENDATIONS

2.1 Members are asked to note the report.

3. CORPORATE PRIORITIES

The report relates to the following corporate priorities

Excellence and Financial Sustainability	✓
Health and Wellbeing	
Place	

Projects relating to People in the Corporate Plan:

People	

4. BACKGROUND TO THE REPORT

4.1 The Treasury Strategy for 2018/19 to 2022/23 was approved by Council on 28 February 2018. The strategy included prudential and treasury indicators, the treasury management strategy, the annual investment strategy, and the annual Minimum Revenue Provision (MRP) Policy.

4.2 A mid-year review of Treasury Management activity was presented to Governance Committee on 22 November 2018. In addition, an assessment of amended investment strategy options for 2018/19 was presented to Council on 5 December 2018. Council approved the addition of LVNAV Money Market Funds to the list of investment counterparties, and an increase in the maximum investment limit for UK local authorities, banks and building societies to £6m (per group or independent institution, as appropriate).

4.3 On 27 February 2019, Council approved the Treasury Management Policy Statement for 2019/20, which included revised prudential and treasury indicators for 2018/19. Where relevant, comparisons with 2018/19 indicators in this outturn report are to those approved most recently.

4.4 A glossary of technical terms used in the report is presented as Appendix H.

5. THE COUNCIL'S CAPITAL EXPENDITURE AND FINANCING

5.1 The Council undertakes capital expenditure on long-term activities. 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.

5.2 The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure for 2018/19.

Table 1 - Capital Expenditure 2018/19	**2018/19 Estimate £000**	**2018/19 Revised £000**	**2018/19 Actual £000**	**2018/19 Variance £000**
2018/19 Capital Programme	8,151	2,898	2,422	(476)
Additional finance lease liability	104	103	0	(103)
Capital Expenditure Total	**8,255**	**3,001**	**2,422**	**(579)**

Additional analysis of the schemes included in the 2018/19 Capital Programme was presented to Cabinet on 19 June 2019 in the report "South Ribble Borough Council Budget Out-turn Report 2018/19".

5.3 Financing of the capital expenditure is shown in the following table.

Table 2 - Capital Financing 2018/19	**2018/19 Estimate £000**	**2018/19 Revised £000**	**2018/19 Actual £000**	**2018/19 Variance £000**
Capital expenditure from Table 1	8,255	3,001	2,422	(579)
Capital Receipts	(450)	(1,152)	(1,151)	1
Grants & Contributions	(1,394)	(849)	(753)	96
Revenue and Reserves	(3,839)	(897)	(518)	379
Net financing needed for year	**2,572**	**103**	**0**	**(103)**

6. THE COUNCIL'S OVERALL BORROWING NEED

6.1 The Council's underlying need to borrow for 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 unfinanced capital expenditure in 2018/19 plus prior years' unfinanced capital expenditure which has not yet been paid for by revenue or other resources. At outturn there was no additional unfinanced capital expenditure in 2018/19.

6.2 Part of the Council's treasury activity is to address the funding requirement for this borrowing need. Depending on the capital expenditure programme, the Council's cash position is organised 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. In 2018/19 it did not prove necessary to borrow for this purpose.

6.3 The CFR is not matched in full by external borrowing, so the Council is said to have under borrowed by using its own cash balances to finance capital expenditure. There is some loss of interest as a result, but had external loans been taken the interest payable would have been at a higher rate. Use of the Council's own cash helps to achieve savings in net interest.

6.4 The Council's underlying borrowing need is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision (MRP), to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can be borrowed and repaid, but this does not change the CFR.

6.5 The total CFR can also be reduced by:

- the application of additional capital financing resources (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

6.6 The 2018/19 MRP Policy (as required by MHCLG Guidance) was approved by Council as part of the Treasury Strategy 2018/19 to 2022/23 on 28 February 2018.

6.7 The Council's CFR for the year is shown in Table 3 below, and represents a key prudential indicator. It includes financing by means of a finance lease for leisure related capital investment, which increases the Council's borrowing need. No borrowing is actually required in respect of the finance lease because this is included in the contract.

Table 3 - Capital Financing Requirement 2018/19	**2018/19 Estimate £000**	**2018/19 Revised £000**	**2018/19 Actual £000**	**2018/19 Variance £000**
Opening CFR	4,722	4,626	4,626	0
Net financing need for the year (Table 2)	2,572	103	0	(103)
Less MRP/VRP	(934)	(886)	(886)	0
Closing CFR	**6,360**	**3,843**	**3,740**	**(103)**

See also Note 35 Capital Expenditure and Financing in the Statement of Accounts 2018/19.

6.8 Borrowing activity is constrained by prudential indicators for gross borrowing and the CFR, and by the authorised limit.

6.9 **Gross borrowing and the CFR.** In order to ensure that borrowing levels are prudent over the medium term and are only for capital purposes, the Council ensures that its gross external borrowing does not, except in the short term, exceed the total of the CFR in the preceding year (2017/18) plus the estimates of any additional CFR for the current (2018/19) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator would allow the Council some flexibility to borrow in advance of its immediate capital needs, but this was not required in 2018/19.

6.10 Table 4 shows the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

Table 4 - Portfolio Position 31 March 2018	2018/19 Estimate £000	2018/19 Revised £000	2018/19 Actual £000	2018/19 Variance £000
Debt at 1 April	0	0	0	0
Other long-term liabilities (OLTL)	749	900	900	0
Total gross debt 1 April	749	900	900	0
Change in Debt	1,750	0	0	0
Change in OLTL	(212)	(213)	(298)	(85)
Expected change in gross debt	1,538	(213)	(298)	(85)
Gross debt 31 March	2,287	687	602	(85)
Capital Financing Requirement (Table 3)	6,360	3,843	3,740	(103)
Under borrowing	**4,073**	**3,156**	**3,138**	**(18)**

6.11 **The authorised limit.** This 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 revised limit set for 2018/19 by Council on 27 February 2019 was £3.687m and actual gross borrowing shown in Table 4 was £0.602m. The Council has maintained gross borrowing within its authorised limit.

6.12 **The operational boundary.** This 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. The revised operational boundary set for 2018/19 was £0.687m and actual gross debt at 31 March 2019 was £0.602m.

6.13 **Actual financing costs as a proportion of net revenue stream.** This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income), against the revenue stream (council tax, business rates, and various Government grants).

Table 5 - Ratio of Financing Costs to Net Revenue Stream 2018/19	2018/19 Estimate %	2018/19 revised %	2018/19 Actual %	2018/19 Variance %
Ratio	7.95	5.59	5.04	-0.55

The actual ratio was lower than estimated in 2018/19 because net financing costs were lower than estimated and the revenue stream was higher.

7. TREASURY POSITION AS AT 31 MARCH 2019

7.1 The Council's treasury management debt and investment position is organised to ensure adequate liquidity for revenue and capital activities, security for investments, and to manage risks within all treasury management activities. Gross debt is shown in Table 4, and Investments (including Cash and Cash equivalents but excluding accrued interest) are shown in Table 6.

Table 6 - Year-End Resources 2018/19	2018/19 Estimated £000	2018/19 Revised £000	2018/19 Actual £000	2018/19 Variance £000
Core Funds/Working Balances	(27,228)	(38,156)	(37,256)	900
Under borrowing (Table 4)	4,073	3,156	3,138	(18)
Investments	**(23,155)**	**(35,000)**	**(34,118)**	**882**

7.2 A detailed analysis of Short Term Investments and Cash and Cash Equivalents is presented as Appendix A. Term Deposits by counterparty are shown in Table 7.

Table 7 - Summary of Term Deposits by Counterparty 31 March 2019	Type	Amount 31 March 2019 £000	Limit £000
Bank of Scotland	Term	2,000	6,000
Goldman Sachs International Bank	Term	4,000	6,000
UK Banks		6,000	
Conwy County Borough Council	Term	2,000	6,000
Hull City Council	Term	2,000	6,000
Lancashire County Council	Term	6,000	6,000
Salford City Council	Term	2,000	6,000
Slough Borough Council	Term	2,000	6,000
Thurrock Borough Council	Term	2,000	6,000
UK Local Authorities		16,000	
Fixed Term Deposits sub total		**22,000**	

7.3 The table confirms that the maximum balance invested with each counterparty complied with the limit approved by Council. Appendix B presents the approved limits for 2018/19.

7.4 Council approved a maximum of £5m should be invested with UK local authorities for more than 365 days and up to two years. No sums were invested for more than 365 days.

Table 8 - Maximum Principal Sums Invested > 365 Days 2018/19	**2018/19 Estimate £000**	**2018/19 Revised £000**	**2018/19 Actual £000**
UK Government	0	0	0
UK Local Authorities	5,000	5,000	0
UK Banks & Building Societies	0	0	0
Non-UK Banks	0	0	0
Total	**5,000**	**5,000**	**0**

8. INVESTMENT PERFORMANCE 2018/19

8.1 Investment returns remained low during 2018/19. When the treasury management strategy for 2018/19 was approved, the expectation was that Bank Rate would rise from 0.50% to 0.75%. At the start of 2018/19, and after UK GDP growth had proved disappointingly weak in the first few months of 2018, the expectation for the timing of this increase was pushed back from May to August 2018. Investment interest rates were therefore on a gently rising trend in the first half of the year after April, in the anticipation that the MPC would raise Bank Rate in August. This duly happened at the MPC meeting on 2 August 2018. During this period, investments were kept in highly liquid accounts in anticipation that rates would be higher later in the year, when placing cash in term deposits would become more attractive.

8.2 Continued uncertainty in the aftermath of the 2008 financial crisis has promoted a cautious approach whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates. The Council has continued to achieve budget savings by maintaining a position of under borrowing, which means that it has used its own cash balances to finance capital expenditure rather than taking external loans.

8.3 **Investment Policy.** The Council's investment policy is governed by MHCLG investment guidance, which has been implemented in the annual investment strategy approved by Council for 2018/19. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data (such as ratings outlooks, credit default swaps, banks share prices etc.). Link Asset Services, the Council's treasury advisors, provide suggested investment durations for the approved counterparties. From time to time, suggested durations reduce after a term deposit has been placed, for instance from twelve to six months, but this did not occur during 2018/19.

8.4 Investment performance for 2018/19 is presented in Table 9.

Table 9 - Investment Performance 2018/19	Average Daily Investment £000	Interest 2018/19 £	Average Rate %
Fixed Term Deposits	18,384	147,963	0.80
Notice Accounts	8,795	78,669	0.89
Call Accounts	2,034	9,505	0.47
Money Market Funds	10,779	66,134	0.61
Debt Management Office DMADF	64	322	0.50
Total	**40,056**	**302,593**	**0.76**

8.5 The average return of 0.76% in 2018/19 compares to the 0.49% achieved in the previous year, and reflects the gradual increase in interest rates. It proved necessary to use the Debt Management Office's Debt Management Account Deposit Facility for short periods when balances with other counterparties had reached the maximum approved by Council. This was avoided later in the year by an increase in the maximum investment per UK bank or local authority from £5m to £6m.

8.6 The average 7-day LIBID for 2018/19 was 0.50%. The target to exceed for 2018/19 was 7-day LIBID plus 15%, which was 0.57%. This was achieved.

8.7 Link Asset Services suggested a budgeted investment earnings rate of 0.60% for 2018/19, based on investment durations of up to three months. Though the Council placed few term deposits in the first half of the year, more cash was invested for durations of up to a year in the second half, and the target was exceeded.

9. MONITORING JUNE QUARTER 2019/20

9.1 Investments as at 30 June 2019 are listed in Appendix D. All investments, which totalled £39.59m, were in accordance with the approved investment strategy and list of counterparties for 2019/20. Of this total, £25.0m was in term deposits and notice accounts, and the balance of £14.59m was in more liquid accounts at lower rates of interest.

9.2 Appendix E presents the approved limits for 2019/20.

10. ADVICE OF LINK ASSET SERVICES

10.1 Link Asset Services' review of the Economy and Interest Rates in 2018/19 is presented as Appendix C.

10.2 A detailed economic commentary on developments during the quarter ended 30 June 2019 is presented as Appendix E.

10.3 Appendix F is a detailed commentary on interest rate forecasts. This includes an updated forecast for the rate of return on cash invested for 2019/20 and subsequent years.

11. CONSULTATION CARRIED OUT AND OUTCOME OF CONSULTATION

11.1 No consultation was undertaken in preparing this report.

12. FINANCIAL IMPLICATIONS

12.1 There are no direct financial implications arising as a result of this report. Variances from the revised budgets for interest receivable and payable for 2018/19 were reflected in the report "South Ribble Borough Council Budget Out-turn Report 2018/19", presented to Cabinet on 19 June 2019.

13. LEGAL IMPLICATIONS

13.1 Presentation of this report is required to comply with the CIPFA Code of Practice on Treasury Management in the Public Services (2017 edition).

14. COMMENTS OF THE STATUTORY FINANCE OFFICER

14.1 There are no financial implications arising directly as a result of this report. All financial implications in respect of treasury management activity arise as a result of the annual Treasury Strategies for 2018/19 and 2019/20 approved previously by Council. This report presents details of actual performance achieved as a result of implementing the approved strategies.

15. COMMENTS OF THE MONITORING OFFICER

15.1 Please see the Legal Implications section above.

16. OTHER IMPLICATIONS

▶ **HR & Organisational Development** ▶ **ICT / Technology** ▶ **Property & Asset Management** ▶ **Risk** ▶ **Equality & Diversity**	Risk is an important issue for Treasury Management activity, and management of risk is at the heart of the Treasury Strategy for each financial year.

17. BACKGROUND DOCUMENTS

- CIPFA Treasury Management in the Public Services: Code of Practice & Cross-Sectoral Guidance Notes (December 2017 edition)
- CIPFA Treasury Management in the Public Services: Guidance Notes for Local Authorities (July 2018 edition)
- CIPFA Prudential Code for Capital Finance in Local Authorities (December 2017 edition)
- CIPFA Standards of Professional Practice: Treasury Management
- MHCLG Guidance on Local Government Investments
- MHCLG Guidance on Minimum Revenue Provision
- Treasury Strategy 2018/19 to 2022/23 (Council 28 February 2018)
- Amended Investment Strategy Options 2018/19 (Council 5 December 2018)
- Treasury Management Policy Statement 2019 (Council 27 February 2019)

18. APPENDICES

Appendix A: Investments as at 31 March 2019
Appendix B: Investment Counterparties 2018/19
Appendix C: Link Asset Services' review of the Economy and Interest Rates
Appendix D: Investments as at 30 June 2019
Appendix E: Investment Counterparties 2019/20
Appendix F: Detailed economic commentary on developments during quarter ended 30 June 2019
Appendix G: Detailed commentary on interest rate forecasts
Appendix H: Glossary of Terms

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Job Title: Interim S151 Officer

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