

REPORT TO	ON
Governance Committee	26 July 2018



TITLE	REPORT OF
Treasury Management Annual Report 2017/18	Deputy Chief Executive (Resources & Transformation)

Is this report confidential?	No
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1. PURPOSE OF THE REPORT

- 1.1 To present the outturn for Treasury Management activity in financial year 2017/18.
- 1.2 To present Treasury Management activity monitoring information for the quarter to 30 June 2018, together with a commentary on issues relating to the economy and updated interest rate forecasts.

2. RECOMMENDATIONS

- 2.1 Members are asked to note the report.

3. EXECUTIVE SUMMARY

- 3.1 All investment activity during 2017/18 complied with the strategy approved by council. An average return of 0.49% was achieved, which exceeded the target rate of 0.24% (being the 7-day LIBID plus 15%).
- 3.2 Investments peaked at £45.1m. At year-end, the total excluding accrued interest was £31.6m.
- 3.3 The average rate earned in the first quarter of 2018/19 has increased to 0.63%, though the average sum invested per day is currently lower than the average for 2017/18.
- 3.4 Officers will aim to identify additional counterparties, in particular money market funds and UK banks, as permitted by the approved investment strategy for 2018/19.

4. CORPORATE PRIORITIES

- 4.1 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	
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5. BACKGROUND TO THE REPORT

- 5.1 The Treasury Strategy for 2017/18 to 2019/20 was presented to Cabinet on 20 February 2017. The strategy included Prudential Indicators, the Treasury Management Strategy, the Annual Investment Strategy, and the Annual Minimum Revenue Provision (MRP) Policy Statement, all of which were approved by Council on 1 March 2017.
- 5.2 Treasury Management activity monitoring reports were presented to Governance Committee meetings of 13 September 2017 and 31 January 2018.
- 5.3 Revised Prudential and Treasury indicators for 2017/18 were included in the Treasury Strategy 2018/19 to 2022/23, which was approved by Council on 28 February 2018. Where relevant, comparisons with 2017/18 indicators in this outturn report are to those approved most recently.

6. TREASURY MANAGEMENT OUTTURN 2017/18

Capital Expenditure 2017/18

- 6.1 The following table compares actual capital expenditure in 2017/18 with the original and revised estimates for the year.

Table 1 - Capital Expenditure 2017/18	2017/18 Estimate £000	2017/18 Revised £000	2017/18 Actual £000	2017/18 Variance £000
2017/18 Capital Programme	4,404	3,004	2,177	(827)
Additional finance lease liability	124	124	257	133
Capital Expenditure Total	4,528	3,128	2,434	(694)

The finance lease liability is in respect of expenditure incurred through the leisure contract.

Capital Financing 2017/18

- 6.2 Table 2 shows the estimated and actual financing of the capital expenditure in Table 1. Net financing represents the expenditure which is financed by an increase in the Capital Financing Requirement. This consists of the increase in the finance lease liability (£0.257m) and prudential borrowing (£0.056m).

Table 2 - Capital Financing 2017/18	2017/18 Estimate £000	2017/18 Revised £000	2017/18 Actual £000	2017/18 Variance £000
Capital Receipts	500	228	174	(54)
Grants & Contributions	1,268	1,659	1,279	(380)
Revenue and Reserves	1,666	832	668	(164)
Net financing needed for year	1,094	409	313	(96)

The Council's borrowing need (the Capital Financing Requirement - CFR)

- 6.3 The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness, and therefore its underlying borrowing need. Any capital expenditure in Table 1 above which has not been paid for immediately will increase the CFR.
- 6.4 The CFR does not increase indefinitely, as the Minimum Revenue Provision (MRP), which is a statutory annual charge, broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used in the provision of services.
- 6.5 The CFR includes any other long-term liabilities (in particular finance leases). These increase the CFR, but include a borrowing facility by the lease provider and so the council is not required to borrow separately for these schemes.
- 6.6 The outturn CFR compared to estimated figures is shown in Table 3:

Table 3 - Capital Financing Requirement 2017/18	2017/18 Estimate £000	2017/18 Revised £000	2017/18 Actual £000	2017/18 Variance £000
Opening CFR	5,146	5,302	5,302	0
Net financing need for the year (Table 2)	1,094	409	313	(96)
Less MRP/VRP	(1,018)	(989)	(989)	0
Closing CFR	5,222	4,722	4,626	(96)

Ratio of financing costs to net revenue stream

- 6.7 This indicator identifies the trend in the cost of capital (borrowing and other long-term obligation costs net of investment income) against the net revenue stream (council tax, business rates, and general government grants).

Table 4 - Ratio of Financing Costs to Net Revenue Stream 2017/18	2017/18 Estimate %	2017/18 Actual %	2017/18 Variance %
Ratio	8.36	7.05	-1.31

- 6.8 The ratio has reduced because financing costs were less than estimated, and the revenue stream was higher than estimated. Interest receivable exceeded the amount estimated when the ratio for the year was calculated, and business rates income (including S31 Grants to finance rates reliefs) exceeded the budgeted income.

Core funds and expected investment balances

- 6.9 The application of resources such as capital receipts and reserves either to finance capital expenditure or to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources, such as asset sales.
- 6.10 Table 5 shows that investments exceeded the forecast by £1.392m.

Table 5 - Year-End Resources 2017/18	2017/18 Revised £000	2017/18 Actual £000	2017/18 Variance £000
Fund balances / reserves	(26,739)	(27,101)	(362)
Capital receipts	(1,856)	(1,932)	(76)
Provisions	(1,200)	(1,700)	(500)
Total core funds	(29,795)	(30,733)	(938)
Working capital*	(4,500)	(4,707)	(207)
Under borrowing (Table 6)	3,973	3,726	(247)
Investments	(30,322)	(31,714)	(1,392)

*Working capital balances shown are estimated year-end; these may be higher mid-year

Portfolio position

- 6.11 Table 6 shows the actual external debt (the treasury management operations) against the underlying capital borrowing need (the Capital Financing Requirement), highlighting under borrowing of £3.726m as at 31 March 2018.

Table 6 - Portfolio Position 31 March 2018	2017/18 Revised £000	2017/18 Actual £000	2017/18 Variance £000
Debt at 1 April	0	0	0
Other long-term liabilities (OLTL)	941	941	0
Total gross debt 1 April	941	941	0
Expected change in Debt	0	0	0
Expected change in OLTL	(192)	(41)	151
Expected change in gross debt	(192)	(41)	151
Gross debt 31 March	749	900	151
Capital Financing Requirement (Table 3)	4,722	4,626	(96)
Under borrowing	3,973	3,726	(247)

6.12 The under borrowing reflects the use of the council's own cash to finance capital expenditure, being a form of internal borrowing, rather than taking external loans from a source such as the Public Works Loan Board. Though there is a loss of interest receivable because the £3.726m cash was not available to invest, the interest that would have been earned would have been a lot lower than the interest payable on the PWLB loans that would have been required to generate the extra cash balance. At present this is the best value use of the council's cash.

Operational Boundary

6.13 The council set a revised Operational Boundary of £0.749m for 2017/18. This is the limit beyond which external debt is not normally expected to exceed. This could be set at a similar figure to the CFR if the council expected to borrow at that level, but the ability to fund under-borrowing from other cash resources meant that for 2017/18 it was set at the estimated level of finance lease debt as at 31 March 2018. Table 6 above shows that the actual debt was £0.900m, so this indicator was exceeded by £0.151m.

Authorised Limit for external debt

6.14 This is a control on the maximum level of borrowing. It represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by full council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

6.15 The revised limit for 2017/18 approved by council was £3.749m, and it was not exceeded.

Investment Performance 2017/18

6.16 Income earned by category of investment is shown in Table 7 following:

Table 7 - Investment Performance 2017/18	Average Daily Investment £000	Interest 2017/18 £	Average Rate %
Fixed Term Deposits	21,526	118,961	0.55
Notice Accounts	5,299	35,559	0.67
Call Accounts	1,847	4,912	0.26
Money Market Funds	7,493	19,688	0.27
Total	36,165	179,120	0.49

- 6.17 No use was made of the government's Debt Management Office DMADF account, which though very secure offers a lower rate of interest for short-term deposits than alternatives such as call accounts and money market funds. Term deposits and notice accounts were used for cash which could be invested for longer periods at higher interest rates.
- 6.18 The average rate earned was 0.49%, which is lower than the 0.57% achieved in 2016/17. Unfortunately all investment counterparties offered lower rates of interest than in the previous financial year.
- 6.19 The performance benchmark is the 7-day London Interbank Bid (LIBID) rate, which averaged 0.21% in 2017/18. The performance target is to achieve a return rate 15% greater than LIBID, so the target for 2017/18 was 0.24% and the actual return of 0.49% exceeded the target.
- 6.20 Investments held as at 31 March 2018, excluding accrued interest, are presented in Appendix A. The list of approved investment categories for 2017/18 is presented as Appendix B.
- 6.21 Table 8 summarises the term deposits at year-end by investment counterparty, and compares the value to the approved maximum. All totals were within the maximum approved, and all investments in 2017/18 complied with the approved policy.

Table 8 - Summary of Term Deposits by Counterparty 31 March 2018	Type	Amount 31 March	
		2018 £000	Limit £000
Bank of Scotland	Term	1,000	5,000
Blackpool Council	Term	2,000	5,000
Cherwell District Council	Term	2,000	5,000
Flintshire County Council	Term	2,000	5,000
Goldman Sachs International Bank	Term	3,000	5,000
Helaba	Term	4,000	4,000
Lancashire County Council	Term	5,000	5,000
Thurrock Borough Council	Term	2,000	5,000
Fixed Term Deposits sub total		21,000	

- 6.22 Though approved investment counterparties included all UK banks with suitable creditworthiness, most of the large banks with suitable credit ratings are not on this list. This is because many of them set high minimum deposit values for local authorities, £20m being typical, and this council would not deposit such a value with one counterparty. Unfortunately this restricts the availability of bank counterparties which can be used for term deposits.
- 6.23 The highest value invested during 2017/18 was £45.1m in February 2018. Such sums are achieved temporarily when the council holds cash such as council tax and business rates, collected on behalf of government and other local authorities, which is paid over to other bodies after being invested for a few days.
- 6.24 Council approved a maximum of £5m which could be invested with UK local authorities for greater than 365 days. Approval of this limit was to enable a higher rate of return to be earned on a limited amount of the council's cash, should a local authority make a worthwhile offer. No sums were invested for more than 365 days in 2017/18.

Table 9 - Maximum Principal Sums Invested > 365 Days 2017/18	2017/18 Estimate £000	2017/18 Revised £000	2017/18 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

7. TREASURY MANAGEMENT ACTIVITY MONITORING 2018/19 – QUARTER 1

- 7.1 Investment performance for the quarter to 30 June 2018 is shown in the following table:

Table 10 - Investment Performance 2018/19	Average Daily Investment £000	Interest to 30 June 2018 £	Average Rate %
Fixed Term Deposits	19,967	32,071	0.65
Notice Accounts	8,176	14,767	0.73
Call Accounts	1,331	1,166	0.36
Money Market Funds	6,486	7,677	0.48
Total	35,960	55,681	0.63

- 7.2 At £35.96m, the average daily investment is currently lower than that for 2017/18, but investments tend to peak later in the year, which increases the average. The average rate of interest achieved for each category is higher than in 2017/18, and the overall average rate is currently 0.63%. No use has been made of the DMO's Debt Management Account Deposit Facility. The average 7-day LIBID rate to the end of June was 0.36%, and the target to exceed was therefore 0.41%.

7.3 A list of investments as at 30 June 2018 is presented as Appendix C, and approved counterparties for 2018/19 as Appendix D. The only change in approved counterparties since 2017/18 was the deletion of variable net asset value (VNAV) Enhanced Money Market Funds as an option, but such EMMFs had not been used by the council.

7.4 The term deposits by counterparty as at 30 June 2018 were as follows:

Table 11 - Summary of Term Deposits by Counterparty 30 June 2018	Amount 30 June 2018	Type	Limit	
			£000	£000
Bank of Scotland	1,000	Term	5,000	
Cherwell District Council	2,000	Term	5,000	
Coventry Building Society	2,000	Term	5,000	
Goldman Sachs International Bank	5,000	Term	5,000	
Helaba	4,000	Term	4,000	
Fixed Term Deposits sub total	14,000			

7.5 All investments complied with council policy and were within the approved maximum limits.

7.6 So far this year, fewer UK local authorities have been willing to take term deposits. When deposits with local authorities have matured, it has sometimes proven necessary to reinvest the cash with other counterparties. If this trend continues, it could become difficult to avoid use of the DMO's DMADF, which pays a lower rate of interest than usually offered by other counterparties for term deposits. The latest indicative interest rates available for the DMADF show that a maximum of 0.45% can be earned on deposits for six months, compared to the average of 0.65% achieved in the year to date for term deposits.

7.7 Officers will aim to avoid use of the DMADF by using additional counterparties permitted by the approved investment strategy. Currently the council uses three money market funds – BlackRock, Federated and Standard Life – but other suitable MMFs are available. Brokers will be consulted to identify suitable UK banks not currently used which will take deposits of £5m or less, as permitted by the approved strategy.

7.8 Use of existing and new MMFs will need to take account of the European Union MMF reforms which will become effective from 21 January 2019. Our treasury advisors, Link Asset Services, will continue to provide advice in respect of the impact of the reforms.

7.9 In Appendix E, Link Asset Services present a detailed economic commentary on developments during the first quarter of 2018/19, provided to them by Capital Economics. Appendix F is Link's detailed commentary on interest rate forecasts. An increase in bank rate to 0.75% is expected before the end of 2018, though the rate is expected to match previous forecasts only during 2021 when it could reach 1.50%.

8. CONSULTATION CARRIED OUT AND OUTCOME OF CONSULTATION

8.1 No consultation has been undertaken in preparing this report.

9. FINANCIAL IMPLICATIONS

9.1 There are no direct financial implications arising as a result of this report.

10. LEGAL IMPLICATIONS

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

11. COMMENTS OF THE STATUTORY FINANCE OFFICER

- 11.1 All financial implications in respect of Treasury Management activity arise as a result of the annual Treasury Strategies for 2017/18 and 2018/19, previously approved by council. This report presents details of actual performance as a result of implementing the approved strategies.

12. COMMENTS OF THE MONITORING OFFICER

- 12.1 Please see the Legal Implication section above.

13. OTHER IMPLICATIONS:

<ul style="list-style-type: none">▶ HR & Organisational Development▶ ICT / Technology▶ Property & Asset Management▶ Risk▶ Equality & Diversity	<p>The Treasury Strategy sets limits on investments in order to manage risks.</p>
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14. BACKGROUND DOCUMENTS

Treasury Strategy 2017/18 to 2019/20	(Council 1/3/17)
Treasury Management Activity Mid-year Review 2017/18	(Governance Committee 13/9/17)
Treasury Management Activity 2017/18 – update	(Governance Committee 31/1/18)
Treasury Strategy 2018/19 to 2022/23	(Council 28/2/18)

15. APPENDICES

Appendix A	List of Investments as at 31 March 2018
Appendix B	Investment Counterparties 2017/18
Appendix C	List of Investments as at 30 June 2018
Appendix D	Investment Counterparties 2018/19
Appendix E	Detailed economic commentary on developments during quarter ended 30/6/18
Appendix F	Detailed commentary on interest rate forecasts

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