# BRIEFING PAPER

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| **REPORT to :** | Audit and Governance Committee |
| **LEAD OFFICER:** | Director of Finance And Customer Services |
| **DATE:** | 16th October 2018 |

**WARD/S AFFECTED:** All

## TREASURY MANAGEMENT REPORT – 2018/19

**Based on monitoring information for the period 1st July 2018 – 30th September 2018**

**1. PURPOSE**
To allow scrutiny of the Treasury Management function.

**2. RECOMMENDATIONS**
It is recommended that Audit and Governance Committee notes the Treasury Management position for the period including the potential for the Council to take more longer term borrowing.

**3. BACKGROUND**

3.1 The Council has previously adopted CIPFA's latest Code of Practice on Treasury Management in the Public Services and associated guidance notes. The Treasury Management Strategy for 2018/19, approved at Finance Council in February 2018, complied with both the CIPFA Code and with Ministry for Housing Communities and Local Government (MHCLG) Guidance on Investments. New CIPFA and MHCLG guidance has been issued and the impact of this is still under review. The CIPFA Code, the Investment Guidance issued by MHCLG and the Internal Audit & Assurance reviews of Treasury Management activities all recommend a strong role for elected members in scrutinising the Treasury Management function of the Council.

3.2 This report summarises the interest rate environment for the period and the borrowing and lending transactions undertaken, together with the Council's overall debt position. It also reports on the position against Treasury and Prudential Indicators established by the Council.

3.3 A glossary of Treasury Management Terms is appended to this paper. .

**4. KEY ISSUES**

4.1 Interest Rates

The Bank of England's Bank Rate was increased in August from 0.50% to 0.75%. There were consequent increases in the quoted rates in financial markets, and in the interest paid on investments by some banks; the rates at which local authorities lend to each other also increased.

This will put pressure on the Council’s Interest Payable budget, which will be reflected in budget monitoring reports.

4.2 Investments Made and Interest Earned

The graph in Appendix 1 shows the weekly movements in totals available for investment, both actuals to date and projections for the rest of the year (adjusted for anticipated borrowing).

Investments made in the period were mainly in “liquid” (instant access) deposits, either bank “call accounts” or Money Market Funds (MMFs). Returns on such MMF holdings are slowly improving, now paying between 0.60% and 0.65%. Bank account rates vary, paying from 0.05% to 0.65%.

For limited periods, funds were also placed with the Government’s Debt Management Office (typically at 0.5%). The other fixed term investments made were:

| Start Date | End Date | Counterparty | Amount | Rate % |
|---|---|---|---|---|
| 14-Aug-18 | 19-Oct-18 | Tameside MBC | £3,000,000 | 0.60 |
| 17-Sep-18 | 15-Oct-18 | Blackpool | £2,000,000 | 0.65 |
| 09-Aug-18 | 07-Sep-18 | Cheltenham BC | £2,000,000 | 0.65 |
| 28-Aug-18 | 05-Sep-18 | Gwynedd | £3,000,000 | 0.68 |
| 03-Sep-18 | 03-Oct-18 | City of Nottingham | £2,000,000 | 0.65 |
| 07-Sep-18 | 14-Dec-18 | National Counties Building Society | £1,000,000 | 0.81 |
| 27-Sep-18 | 26-Oct-18 | Thurrock MBC | £3,000,000 | 0.80 |

At 30th September, the Council had approximately £24.6 M invested, compared to £21.4 M at the start of the period. Appendix 2 shows the breakdown of the investment balance at the end of the period.

The Council’s investment return over the period was approximately 0.56%.

For comparison, benchmark LIBID (London Interbank Bid) rates remained fairly stable; the average rate for 1 month’s lending was around 0.54% (holding at around 0.6% at period end), and for 3 months it was around 0.66% (and holding at around 0.68% at period end).

4.3 Borrowing Rates

The cost of long term borrowing through the PWLB (Public Works Loan Board) is linked to Central Government's own borrowing costs. Average PWLB borrowing rates remain historically low, but moved up last autumn and winter, and have fluctuated since then. Although we have not taken new long term loans, if we were to do so, the cost would be higher than a year ago. Over the last quarter rates have stabilised overall, and new 5 year “certainty” loans cost around 1.9% (usually ranging between 1.8% and 2.0%), while loans from 20 to 50 years cost around 2.65% (ranging between 2.5% and 2.8%).

Short term borrowing rates, based on loans from other councils, remain historically low. They are now starting to move steadily, albeit slowly, upwards. At present 3 month loans cost around 0.80%, while loans from 6 months to 1 year are between 0.85% and 1.15%. Though the broad trend has been, and is expected to continue slowly upwards, it is unclear how rates will move in the run up to Brexit.

4.4 Borrowing and Lending in the 3 month period

The Council's CFR (Capital Financing Requirement) is the key measure of the Council's borrowing **need** in the long term. It is

(a) the accumulated need to borrow **to finance capital spend** (not funded from grants, etc.) ***less***
(b) the accumulated Minimum Revenue Provision (MRP) charges already made - councils must make a prudent MRP charge in their accounts each year, to finance their debt - ***less***
(c) any capital receipts applied to finance outstanding debt.

and therefore tends to increase if capital spend financed from borrowing exceeds MRP.

The Council's **actual** long term debt is around £92 M below the CFR – the gap widens as long term debt is repaid, and the Council has taken no new long term borrowing for several years, and is repaying existing debt at maturity.

We are effectively using "internal borrowing" from available revenue cash balances to part cover this gap. Two benefits of this are:
(a) a net saving on interest (as long term borrowing costs more than investments earn), and
(b) smaller balances held, so a lower risk from default on funds invested.

The rest of the gap is covered by taking enough short term borrowing to ensure that the Council has sufficient funds to pay its liabilities and commitments, and to anticipate future borrowing needs.

Over the period, there was an increase in short term borrowing of £3M, as loans of £28M were repaid and **£31M of new loans** were taken (listed below).

| **New loans taken in the period** | | | | |
|---|---|---|---|---|
| **Start Date** | **End Date** | **Counterparty** | **Amount £** | **Rate** |
| 27/07/2018 | 31/07/2018 | Thurrock District Council | 3,000,000 | 0.42% |
| 30/07/2018 | 28/02/2019 | Kent Police | 3,000,000 | 0.75% |
| 31/07/2018 | 31/01/2019 | Middlesbrough/Teeside Pension Fund | 10,000,000 | 0.75% |
| 07/08/2018 | 29/04/2019 | Gwent Police | 3,000,000 | 0.85% |
| 24/09/2018 | 25/03/2019 | Kent Police | 3,000,000 | 0.80% |
| 27/09/2018 | 08/03/2019 | London Borough of Newham | 5,000,000 | 0.68% |
| 28/09/2018 | 28/03/2019 | Tendring District Council | 4,000,000 | 0.68% |
| | | | **31,000,000** | |

| **Future deals already agreed by end of period** | | | | |
|---|---|---|---|---|
| **Start Date** | **End Date** | **Counterparty** | **Amount £** | **Rate** |
| 18/10/2018 | 18/02/2019 | Basildon District Council | 3,000,000 | 0.85% |
| 29/10/2018 | 29/01/2019 | Preston City Council | 3,000,000 | 0.77% |
| 01/11/2018 | 01/05/2019 | Tendring District Council | 2,000,000 | 0.85% |
| | | | **8,000,000** | |

4.5 Current debt outstanding -

The key elements of long term borrowing set out below are:

(a) £18M classed as bonds, borrowed from the money markets, largely in the form of "LOBO"

(Lender Option, Borrower Option) debt. The individual loans remaining range from 4.35% to 4.75%, at an average of around 4.4%

(b) £104M borrowed from the PWLB at fixed rates, at an overall average rate of around 4.2%. Loans repayable on maturity range from 3.06% to 7.875%, and EIP (Equal Instalment of Principal) loans from 1.94% to 3.77%.

(c) Debt managed by Lancashire County Council after Local Government Reorganisation, which is repaid in quarterly instalments across the year, charged provisionally at 2%.

(d) Debt recognised on the balance sheet as a result of accounting adjustments in respect of bringing into use school buildings financed through Public Finance Initiative (PFI) arrangements. The Council's effective control over, and use of these assets is thereby shown "on balance sheet", with corresponding adjustments to the debt. This does not add to the costs faced by the Council Tax payer as these payments made to the PFI contractor are largely offset by PFI grant funding from the Government.

| | 30th June 2018 | | 30th Sept 2018 | |
|---|---|---|---|---|
| . | £000 | £000 | £000 | £000 |
| TEMPORARY DEBT | | | | |
| Less than 3 months | 0 | | 0 | |
| Greater than 3 months (full duration) | 69,000 | | 72,000 | |
| | | 69,000 | | 72,000 |
| LONGER TERM DEBT | | | | |
| Bonds | 18,003 | | 18,003 | |
| Mortgages | 17 | | 17 | |
| PWLB | 103,783 | | 103,783 | |
| Stock & Annuities | 258 | | 258 | |
| | | 122,061 | | 122,061 |
| Lancashire County Council transferred debt | | 15,352 | | 15,045 |
| Recognition of Debt re PFI Arrangements | | 66,419 | | 65,990 |
| **TOTAL DEBT** | | **272,832** | | **275,096** |
| Less: Temporary Lending - fixed term | | (12,000) | | (11,000) |
| - instant access | | (9,441) | | (13,623) |
| **NET DEBT** | | **251,391** | | **250,473** |

4.6 Issues to note in the period

Over the period as a whole, net borrowing was fairly stable. Investments have been, and will continue to be kept short term, and mainly in liquid deposits.

As noted above, interest rates, while both low and volatile, have tended to be moving upwards. This increases the possibility that it may be in the Council's interest in the medium to longer term, to move towards taking more long term borrowing. Such a decision depends on a view on likely future interest rates - both for borrowing and investment.

Future rates will always be uncertain, and any such change would only be adopted after extensive deliberation and support from the Council's treasury advisers, Arlingclose. This would be a departure from the approach taken in the last few years, which has focussed entirely on internal borrowing and short term borrowing and could result in short run pressure on interest budgets.

4.7 Performance against Prudential and Treasury Indicators

Appendix 3 shows the current position against the Prudential and Treasury Indicators set by the Council for the previous and current year.

Movements in the key indicator – Overall Borrowing against Borrowing Limits – are shown as the first graph in Appendix 4. Our total borrowing at 30th September 2018 was, at £275.1M, which is within our Operational and Authorised Borrowing Limits for 2018/19 (£309.5M and £319.5M respectively). The Authorised Borrowing Limit is the key Prudential Indicator - loans from the PWLB cannot be taken if this Limit is (or would be caused to be) breached.

This total debt includes the impact on the balance sheet of the recognition of assets that have been financed through PFI. The accounting adjustments are designed to show our effective long term control over the assets concerned, and the "indebtedness" arising from financing the cost of them. They do not add to the "bottom line" cost met by the Council Tax payer.

The Council still holds a large part of its debt portfolio in loans of less than a year's duration - short term loans are currently the best value way to funding marginal changes in its debt.

Interest Risk Exposures

Our **Variable Interest Rate Exposure** (see second graph at Appendix 4) ended the period at £60.4M, against the **limit** set for this year of £95M.

This indicator exists to ensure that the Council does not become over-exposed to changes in interest rates impacting adversely on its revenue budget. The limit is set to allow for short as well as long term borrowing, and takes:

(a) all variable elements of borrowing (including short term borrowing – up to 364 days – and any LOBO debt at risk of being called in the year), which is then offset by
(b) any lending (up to 364 days).

Our **Fixed Interest Rate Exposure** was around £109M, against the **limit** of £217.5M. This indicator effectively mirrors the previous indicator, tracking the Council's position in terms of how much of the debt will **not** vary as interest rates move. The historically low interest rates prevailing over recent decades led the Council to hold a large part of its debt in this way.

This limit was set to allow for the possibility of higher levels of new long term, fixed rate borrowing, which have not been taken.

**5. POLICY IMPLICATIONS** None

**6. FINANCIAL IMPLICATIONS**

The financial implications arising from Treasury Management activities are reflected in the Council's overall Budget Strategy, and in ongoing budget monitoring throughout the year.

**7. LEGAL IMPLICATIONS**

The report is in accordance with the CIPFA code and therefore is in accordance with the Financial Procedure Rules under the Council's Constitution.

**8. RESOURCE IMPLICATIONS** None

**9. CONSULTATIONS** None

**10. STATEMENT OF COMPLIANCE**

The recommendations are made further to advice from the Monitoring Officer and the Section 151

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| Officer has confirmed that they do not incur unlawful expenditure. They are also compliant with equality legislation and an equality analysis and impact assessment has been considered. The recommendations reflect the core principles of good governance set out in the Council's Code of Corporate Governance. |

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| **VERSION:** | **0.02** |

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| **CONTACT OFFICER:** | Ron Turvey- Deputy Finance Manager extn 5303<br><br>Louise Mattinson Director of Finance & Customer Services extn 5600 |
| **DATE:** | 2nd October 2018 |
| **BACKGROUND PAPERS:** | CIPFA Guidance - CLG Investment Guidance - Council Treasury Management Strategy approved Finance Council 26th February 2018 |