BRIEFING PAPER

REPORT to :	Audit and Governance Committee
LEAD OFFICER:	Director of Finance And Customer Services
DATE:	15th January 2019

WARD/S AFFECTED: All

TREASURY MANAGEMENT REPORT – 2018/19

Based on monitoring information for the period 1st October – 15th December 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, and the draft Treasury Management Strategy for 2019/20, appended to this report.

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.

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 Bank of England Bank Rate

The Bank of England's Bank Rate held steady at 0.75%, having been increased in August.

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). These increased significantly in December after £35M was borrowed from the Public Works Loans Board (PWLB) – see paragraph 4.5 below.

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 just under 0.70%. 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 (at 0.5%). The other fixed term investments made were:

Start Date	End Date	Counterparty	Amount	Rate %
16-Oct-18	16-Jan-19	Thurrock MBC	£2,000,000	0.81
26-Oct-18	31-Jan-19	Thurrock MBC	£3,000,000	0.80
31-Oct-18	25-Jan-19	Barking and Dagenham	£3,000,000	0.80
31-Oct-18	30-Nov-18	Gwynedd Council	£3,000,000	0.68
01-Nov-18	03-Dec-18	Cornwall Council	£3,000,000	0.50
15-Nov-18	31-Jan-19	Conwy Council	£2,000,000	0.80
29-Nov-18	31-Jan-19	Conwy Council	£2,000,000	0.80
03-Dec-18	25-Jan-19	Cornwall Council	£3,000,000	0.68
14-Dec-18	27-Feb-19	Harrow Council	£5,000,000	0.80
14-Dec-18	27-Feb-19	Eastleigh District Council	£5,000,000	0.80
14-Dec-18	27-Feb-19	Dumfries & Galloway	£5,000,000	0.75
14-Dec-18	22-Mar-19	National Counties Building Society	£1,000,000	0.83

At 15th December, the Council had approximately £65.5 M invested, compared to £24.6 M at the start of the period. Appendix 2 shows the breakdown of the closing investment balance

The Council's investment return over the period was approximately 0.70%.

For comparison, benchmark LIBID (London Interbank Bid) rates were
(a) 1 month lending - stable at around 0.6%
(b) 3 month lending - rising over the period, averaging 0.73% and closing at around 0.78%

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.

General market uncertainty in early December prompted a significant fall in PWLB rates, as funds shifted out of stocks and shares and into government debt. The 8 year gilt yield graph below gives an indication of the general pattern of movement in rates, which was significant enough to prompt the Council, working in conjunction with our treasury advisers, Arlingclose, to take a significant amount of new PWLB borrowing, as part of a considered switch from solely taking short term loans to take on more longer term debt.

The cost of short term borrowing, based on loans from other councils, tended to move up across the period, with loans from 3 months out to a year being priced at from 0.80% to 1.10%

Though the broad trend in interest rates has been, and is expected to continue slowly upwards, it is unclear how rates will move in the run up to Brexit.

4.4 Short Term Borrowing 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 significantly below the CFR – the gap has widened as long term debt has been repaid and no new long term borrowing has been taken for several years.
We have been using "internal borrowing" from available revenue cash balances to partly cover this gap. The remaining gap has been 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. This has resulted in net interest savings.

Up to the end of November, there was an increase in short term borrowing of £6M, as loans of £21M were repaid and £27M of new loans were taken (listed below).

New short term loans taken in the period

Start Date	End Date	Counterparty	Amount £	Rate
16/10/2018	18/03/2019	Harlow District Council	2,000,000	0.85%
18/10/2018	18/02/2019	Basildon District Council	3,000,000	0.85%
26/10/2018	27/03/2019	London Borough of Islington	5,000,000	0.90%
29/10/2018	29/01/2019	Preston City Council	3,000,000	0.77%
31/10/2018	25/03/2019	London Borough of Haringey	5,000,000	0.83%
01/11/2018	01/05/2019	Tendring District Council	2,000,000	0.85%
27/11/2018	26/11/2019	West Yorkshire Combined Authority	7,000,000	1.05%
			27,000,000	

4.5 New PWLB Loans taken -

With the wider interest rate market pointing towards future increases in rates, as noted at each Audit Committee meeting in this financial year, the Council has been considering the move towards taking more longer term borrowing rates, and the time to do so, working closely with the Council's treasury advisers, Arlingclose.

As a result of the significant fall in PWLB rates in early December, a series of new PWLB EIP (Equal Instalment of Principal) loans have therefore been taken :

loan start date	Value £	Maturity date	Duration (years)	Rate
07/12/18	10,000,000	30/09/28	10	1.74%
10/12/18	10,000,000	30/09/33	15	1.88%
12/12/18	5,000,000	30/09/30	12	1.73%
13/12/18	10,000,000	30/09/35	17	1.92%

The loans taken were structured to address anticipated future borrowing needs, which are highest over the next 10 to 20 years.

4.6 Current debt outstanding -

	30th Sept 2018		15th Dec 2018	
.	£000	£000	£000	£000
TEMPORARY DEBT				
Less than 3 months	0		3,000	
Greater than 3 months (full duration)	72,000		75,000	
		72,000		78,000
LONGER TERM DEBT				
Bonds	18,003		18,003	
Mortgages	17		17	
PWLB	103,783		138,002	
Stock & Annuities	258		258	
		122,061		156,280
Lancashire County Council transferred debt		15,045		15,045
Recognition of Debt re PFI Arrangements		65,990		65,703
TOTAL DEBT		**275,096**		**315,028**
Less: Temporary Lending - fixed term		(11,000)		(45,575)
- instant access		(13,623)		(19,950)
NET DEBT		**250,473**		**249,503**

The key elements of long term borrowing set out above 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) £138M borrowed from the PWLB at fixed rates, at an overall average rate of around 4%. Loans repayable on maturity range from 3.06% to 7.875%, and EIP (Equal Instalment of Principal) loans from 1.73% 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.

4.7 Treasury Management Strategy for 2019/20

Working under new guidance from MHCLG and CIPFA, the Council will increase the focus of its Capital Strategy and Investment Strategy (including Non-Treasury Investments) at full Council, and will take its Treasury Management Strategy to Executive Board. A draft of the Strategy for 2019/20 is included at Appendix 3.

4.8 Performance against Prudential and Treasury Indicators

Appendix 4 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 5. Our total borrowing at 15th December 2018 was, at £315M, which is above our Operational and below our 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 still represent a cheap way to funding marginal changes in its debt.

Interest Risk Exposures

Our **Variable Interest Rate Exposure** (see second graph at Appendix 5) ended the period at £25.5M, 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 £143M, 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 much higher levels of new long term, fixed rate borrowing. Though the £35M taken has moved this indicator upwards, there are still significant levels of short term debt.

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 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.

VERSION:	**0.02**

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DATE:	21st December 2018
BACKGROUND PAPERS:	CIPFA Guidance - CLG Investment Guidance - Council Treasury Management Strategy approved Finance Council 26th February 2018