Agenda Item 8

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Ward(s) affected	The annual report covers the whole District

Subject	Treasury Management – Annual Report and Prudential Indicators – 2018/19

RECOMMENDATIONS

1) To receive the Treasury Management Annual Outturn report for the financial year ended 31st March 2019 and note the performance against the prudential indicators as detailed in Appendix A.

2) To commend the report to Council making any other relevant recommendations and observations as Members see fit.

EXECUTIVE SUMMARY

Treasury management is the control and management of all the Council's cash, regardless of its source. It covers management of the daily cash position, investments and borrowings. Officers carry out this function within the parameters set by the Council each year in the Treasury Management Strategy Report.

This report reviews the performance of the Prudential Indicators and Treasury Management Strategy and Annual Plan 2018/19 as agreed by Council on 20th February 2018.

The report meets the requirements of both the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code). The Council is required to comply with both Codes through Regulations issued under the Local Government Act 2003. The primary requirements of the Codes are the:

- Creation and maintenance of a Treasury Management Policy Statement (TMPS) that sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices (TMPs) that

set out the manner in which the Council will seek to achieve those policies and objectives.

- Receipt by Council of an annual strategy report (20/02/18) for the year, a mid-year treasury update report (04/12/18) and a subsequent annual review report (this report) after the end of the financial year.

The regulatory environment places responsibility on Members' for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by Members.

Council have delegated the responsibilities for implementing and monitoring treasury management policies and practices to the Audit Committee and for the operation and administration of treasury management decisions to the Deputy Chief Executive (Section 151 Officer), who will act in accordance with the organisation's Treasury Management Policy Statement and TMP's, and CIPFA's Standard of Professional Practice on Treasury Management.

The Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit Committee before they were reported to Council.

In summary, the Council's in-house team together with some externally managed funds achieved a rate of return on investments of 1.57%. The Council achieved an overall return of £417,819 in 2018/19 approximately £93,000 above budget. Investment balances, at balance sheet dates, increased from £13.706m (31/03/18) to £14.497m (31/03/19). The 2018/19 financial year continued the challenging environment of previous years with low investment returns and continuing counterparty risk.

The Council borrowed £52.85m from the Public Works Loans Board (PWLB) during 2018/19.

In conducting the treasury management activities of the Council there were no breaches of the agreed Strategy and the in-house team did not exceed or operated within the Prudential Indicators set by Council.

CORPORATE PRIORITY OUTCOMES

This report is an update on the Council's Prudential Indicators and treasury operations as contained in the Treasury Management Strategy for 2018/19.

The Committee has the authority to determine Recommendation 1 and Council has the authority to determine Recommendation 2.

1. **BACKGROUND/INTRODUCTION**

1.1 Treasury management is defined as:

"The management of the local authority's cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.2 The annual treasury management outturn report for 2018/19 covers:

- The economy and interest rates
- The Council's capital expenditure and financing
- Investment rates
- Borrowing strategy
- Borrowing outturn
- Compliance with Prudential and Treasury Management Indicators (Appendix A)
- Investment strategy
- Investment outturn
- Debt rescheduling
- Borrowing in advance of need
- Other issues
- List of the 9 Prudential Indicators (Appendix B)

2. **The economy and interest rates in 2018/19**

2.1 Investment returns remained low during 2018/19. The expectation for interest rates within the treasury management strategy for 2018/19 was that Bank Rate would rise from 0.50% to 0.75%. At the start of 2018/19, and after UK Gross Domestic Product (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 anticipation that the Monetary Policy Committee (MPC) would raise Bank Rate in August. This duly happened at the MPC meeting on 2nd August 2018.

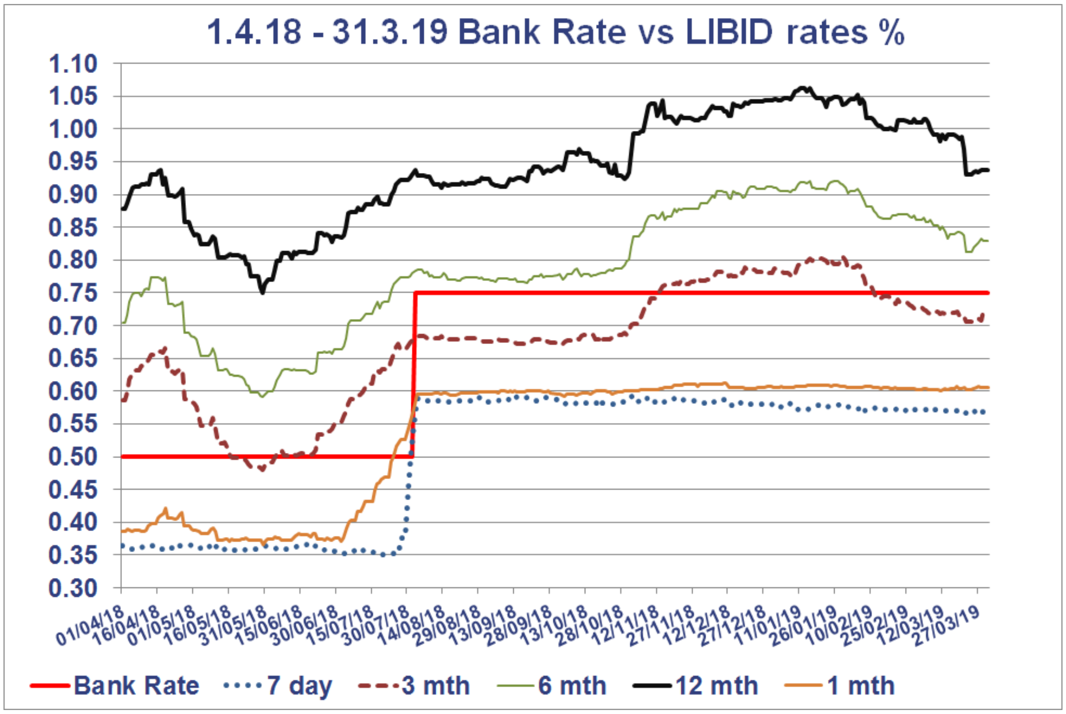
2.2 It was not expected that the MPC would raise Bank Rate again during 2018/19 after August in view of the fact that the UK was entering into a time of major uncertainty with Brexit due in March 2019.

2.3 Investment rates were little changed during August to October but rose sharply after the MPC meeting of 1st November. The Committee was unexpectedly hawkish about their perception of building inflationary pressures, particularly from rising wages. However, weak GDP growth data after December, plus increasing concerns generated by Brexit, resulted in investment rates falling back again.

2.4 This Council does not have sufficient cash balances to be able to place deposits for more than 1-2 months so cannot take the opportunity of earning higher rates from longer deposits. However, when Bank Rate went up in August, its investment returns also improved from deposits for periods up to 1-2 months.

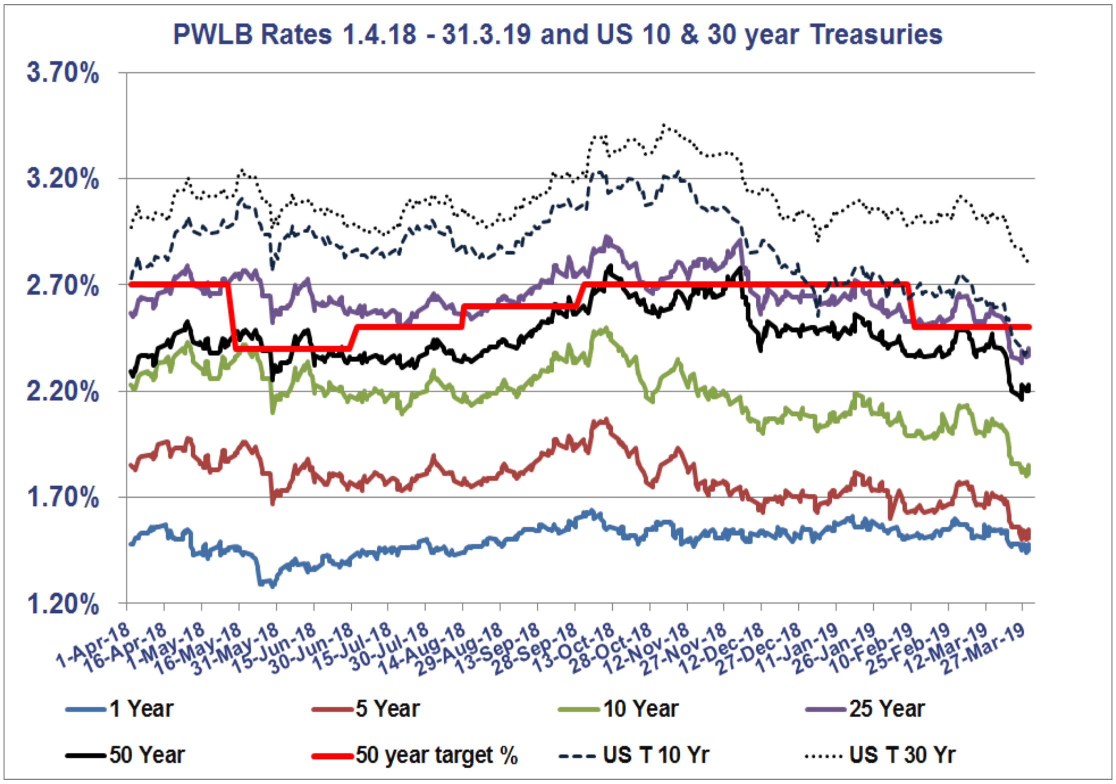
2.5 Continued uncertainty in the aftermath of the 2008 financial crisis has promoted a cautious approach whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

2.6 **Bank Rate v London Interbank BID (LIBID) investment rates**



2.7 **Borrowing PWLB (Certainty Borrowing Rates)**

Since PWLB rates peaked during October 2018, most PWLB rates have been on a general downward trend, though longer term rates did spike upwards again during December, and, apart from the 1 year rate, reached lows for the year at the end of March. There was a significant level of correlation between movements in US Treasury yields and UK gilt yields, which determine PWLB rates. The Federal Reserve (Fed) in America increased the Federal Rate four times in 2018, making nine increases in all in this cycle, to reach 2.25% – 2.50% in December. However, it had been giving forward guidance that rates could go up to nearly 3.50%. These rate increases and guidance caused Treasury yields to also move up. However financial markets considered by December 2018, that the Fed had gone too far, and discounted its expectations of further increases. Since then, the Fed has also come round to the view that there are probably going to be no more increases in this cycle. The issue now is how many cuts in the Federal Rate there will be and how soon, in order to support economic growth in the US. But weak growth now also looks to be the outlook for China and the EU so this will mean that world growth as a whole will be weak. Treasury yields have therefore fallen sharply during 2019 and gilt yields/PWLB rates have also fallen.



3. **Capital Expenditure and Financing 2018/19**

3.1 The Council finances capital expenditure resulting in an increase in long-term assets. These may either be;

- Financed immediately through the application of capital receipts, capital grants or contributions from revenue expenditure, or
- If insufficient financing is available the expenditure will give rise to a borrowing requirement

3.2 In 2018/19, major projects acquired or completed include the Alverston Leys, Stratford-upon-Avon (£16.2m) which was acquired by MOVA Properties, via the purchase of equity shares and loans provided by MVDC. Whilst Quadrangle based in Redhill (£22.0m) and Touristik House based in Dorking (£14.5m) were acquired direct by MVDC. The borrowing requirement during 2018/19 was £52.85m (2017/18: £43.439m), of which £52.85m (2017/18: £40m) was borrowed from the Public Works Loan Board (PWLB) and the remainder was financed through internal borrowing against earmarked reserves that will need to be replenished in future years.

In 18/19 the Council has a capital programme of £141.6 million and as at 31 March 2019 there is a projected £8.0 million net underspend (5.7%) which mostly relates to the Asset Investment Strategy (AIS). No further capital spending will be undertaken on the AIS and therefore no further borrowing will be required for this project.

3.3 The table below shows how capital expenditure was financed over the past two years. Members approved the carry forward to 2018/19 of £119k (2017/18: £579k) capital minor works scheme provision at the Cabinet meeting on 26th June 2018.

	2017/18 Actual £000	2018/19 Projection £000	2018/19 Actual £000
Total capital expenditure	**48,792**	**57,592**	**60,104**
Resourced by :			
Capital receipts	2,768	3,147	1,463
Capital grants & contributions	2,526	1,595	1,012
Borrowing	43,498	52,850	52,850
Total Resources Applied	**48,792**	**57,592**	**55,325**

4. Investment Rates in 2018/19

4.1 The market interest rates at the end of each financial year are shown below. As can be seen rates in 2018/19 are gradually increasing. This is as a result of a Base Rate increase on 2nd August 2018 by 0.25% (to 0.75%).

4.2 Money Market Investment Rates (Average):

Notice	2016/17 %	2017/18 %	2018/19 %
7 Day	0.11	0.36	0.57
1 Month	0.13	0.39	0.61
3 Months	0.21	0.59	0.72
6 Months	0.37	0.70	0.83
1 Year	0.59	0.88	0.94

5. Borrowing Strategy for 2018/19

5.1 The major borrowing requirement objectives to be followed in 2018/19 were;

- To forecast average future interest rates and movements in future interest rates.
- To manage the Council's debt ensuring prompt payment of interest and principal on the due dates.
- To secure the cheapest cost for financing capital schemes commensurate with future risk.

5.2 The Council greatly values revenue budget stability and will therefore borrow the majority of its long-term funding needs at long-term fixed rates of interest. Short-term and variable rate loans will only be borrowed to the extent that they either offset short-term and variable rate investments or can be shown to produce revenue savings.

5.3 The Council commenced borrowing in 2016/17. There was a further borrowing requirement in 2018/19 to fund the capital programme. This is reflected in the higher Operational Boundary and Affordable Limits set out against Performance Indicators 5 and 6 (Appendix A).

6. Borrowing Outturn for 2018/19

6.1 The Council raised funds during 2018/19 through the Public Works Loans Board (PWLB).

6.2 The following loans were taken out during the year:-

Lender	Principal (£)	Type	Interest Rate (%)	Term (Maturity Loan)
PWLB	16,500,000	Fixed interest rate	2.39	50 years
PWLB	22,000,000	Fixed interest rate	2.35	50 years
PWLB	14,350,000	Fixed interest rate	2.40	10 years

7. Compliance with Prudential and Treasury Management Indicators

7.1 During the financial year the Council operated within the Prudential and Treasury Management Indicators 2018/19 – 2020/21 and Treasury Management Strategy and Plan 2018/19 as agreed by Council on 20th February 2018. The outturn for the Prudential and Treasury Management Indicators is detailed in Appendix A of this report.

8. Investment Strategy for 2018/19

8.1 The Investment Strategy's primary objectives are safeguarding the re-payment of the principal and interest of its investments on a timely basis first and ensuring adequate liquidity second, with the investment return being the third objective.

8.1.1 The Financial Scene Setting Report 2019/20 – 2021/22, approved in November 2018, further to the above, seeks to improve returns on investment - without compromising unduly on the security and liquidity of our investments, we will seek to diversify in search of a better yield, with particular consideration of property and property related funds.

8.2 The Asset Investment Strategy completed it property purchases in the year and is on track to deliver the income required to support the delivery of our Council servicers.

8.4 The Council predominantly manages its treasury management investments in-house and invests with the institutions listed in the Council's approved lending list. Following the increase in planned capital spend as a consequence of the AIS, the Council now primarily invests for a range of periods less than two months dependent on the Council's cash flows, its interest rate view and the rates of interest on offer at the time.

8.5 The expectation for interest rates within the Strategy for 2018/19 anticipated an increase in the Bank Rate to 0.75%. This was borne out and the Bank Rate actually rose by 0.25% (to 0.75%) on 2nd August 2018. Investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

8.6 No institutions in which investments were made during 2018/19 had any difficulty in repaying principal and interest in full during the year.

9. Investment Outturn for 2018/19

9.1 The Council's Investment Policy is governed by the Ministry of Housing, Communities and Local Government (MHCLG) guidance, which has been implemented in the annual investment strategy approved by Council on 20th February 2018. This Policy sets out the approach for selecting investment counterparties, and is 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. Counterparties are selected and limits applied using rating criteria. The application of the Council's minimum criteria will apply to the lowest available rating for any institution. For instance if an institution is rated by two agencies, one meets the Council's criteria, the other does not, the institution will fall outside the lending criteria. This is in compliance with the CIPFA Treasury Management Code of Practice. Credit rating information is supplied by our treasury management advisor (Link Asset Services, Treasury Solutions).

9.2 Detailed below is the result of the investment strategy undertaken by the Council.

Internally Managed Funds

9.3 The Council maintained its investment activities during the year, as agreed by Council on 20th February 2018.

9.4 During the year all investments were made in full compliance with the Council's treasury management policies and practices and the Council had no liquidity difficulties.

9.5 The limit to be placed, with each counterparty, remained at £7.5 million. The Council also operated a 'group limit', whereby the collective investment exposure to individual banks within the same banking group was restricted to a group total set also at £7.5 million.

9.6 The analysis below shows the activity undertaken on internally managed funds during 2018/19.

	£
Balance outstanding (at 01/04/18)	13,706,000
Investments made during the year	221,885,000
Upward revaluation of CCLA Property Fund investment (at 31/03/19)	96,000
	235,687,000

Less: Investments maturing during the year	221,190,000
Balance outstanding (at 31/03/19)	14,497,000

9.7 These investments generated interest of approximately £417,800 in the year (£374,000 in 2017/18), gross of all associated charges against a budget of £325,000. As referred to in paragraphs 8.3 and 8.4 agreement was given to increased licence in terms of the scope and range of Council investments. During 2018/19 funds were moved from short-term investments where interest rates were performing at historically low levels. These funds were re-invested in, better performing, property purchases that generated a rental income but meant that there was less to invest in financial instruments. A proportion of investment income is received from short-term investments (investments that mature in, or are held for, 12 months or less). Also good returns are still being achieved on the investment of £5m that was made in the CCLA Property Fund on 30th June 2013 (refer to paragraph 9.10).

	Original Estimate 2018/19 £	Actual Outturn 2018/19 £	Variance 2018/19 £
Internally Managed Funds	325,000	417,819	92,819

9.8 Mole Valley achieved a rate of return of 1.57% on its internally managed funds during the year, this was based on an average fund value of approximately £26,639,000. The formal method used to compare performance is to contrast the rate of return against the average uncompounded 7-day LIBID (London Interbank BID) rate (0.51% for 2018/19). The investment in the CCLA Property Fund, previously alluded to, has significantly enhanced the return on internally/externally managed funds when compared to the benchmark.

9.9 Detailed below is the result of the investment strategy undertaken by the Council.

Funds	Average Fund Value	Rate of Return	Benchmark Return *
Internally / Externally Managed	£26,639,000	1.57%	0.51%

* 7-day LIBID uncompounded 0.5068%

The uncompounded rates are for internally managed funds and exclude the roll-up of principal and interest. Upon maturity of the investment, interest is repaid with the original principal sum.

9.10 Externally Managed Funds – Churches, Charities and Local Authorities (CCLA)

9.11 On 30th June 2013 the Council invested £5m in the Churches, Charities and Local Authorities (CCLA) Property Fund. To realise the full potential of this investment it should be considered as a medium to long term placement. Income is received quarterly and in the current economic climate very good yields are still being achieved.

9.12 The Fund offers all of the advantages of a professionally managed property portfolio, with broadly diversified exposure to high quality properties in the strongest areas of the market. The Fund is a high quality, well diversified commercial and industrial property portfolio. There is a focus on delivering attractive income returns and the Fund is actively managed to add value.

9.13 CCLA has been appointed by the Local Authorities' Mutual Investment Trust (LAMIT) to manage and administer the Local Authorities' Property Fund. LAMIT was established approximately 30 years ago to provide investment services for local authorities in the UK. It is controlled by Members and Officers appointed by the Associations of Local Authorities in the United Kingdom and by Trust Members representing the Funds' unit holders.

9.14 Excellent returns of 4.98% were achieved from this Fund during the year. With the property market remaining buoyant it is anticipated that these returns will continue during 2019/20.

10. Debt rescheduling

10.1 As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

10.2 The reasons for any rescheduling to take place will include:

- the generation of cash savings and/or discounted cash flow savings;
- helping to fulfil the treasury strategy;
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

10.3 Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on the current debt.

10.4 All rescheduling will be reported to the Council, at the earliest meeting following its action.

10.5 No rescheduling was undertaken during 2018/19.

11. Borrowing in advance of need

11.1 The Council has not borrowed more than, or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed.

12. Other issues

12.1 UK Banks – ring fencing

12.2 The largest UK banks, those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits, are required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as "ring-fencing". Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

12.3 Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank (RFB) will be focused on lower risk, day-to-day core transactions, whilst more complex and "riskier" activities are required to be housed in a separate entity, a non-ring-fenced bank (NRFB). This is intended to ensure that an entity's core activities are not adversely affected by the acts or omissions of other members of its group.

12.4 While the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The Council will continue to assess the newly formed entities in the same way that it does others and those with sufficiently high ratings will be considered for investment purposes.

12.5 IFRS9 (Financial Instruments) Accounting Standard

12.6 This accounting standard came into effect on 1st April 2018. It means that the category of investments valued under the available for sale category will be removed and any potential fluctuations in market valuations may impact onto the Surplus or Deficit on the Provision of Services, rather than being held on the balance sheet. This change is unlikely to materially affect the commonly used types of treasury management investments but more specialist types of investments e.g. pooled funds, commercial investments are likely to be impacted.

12.7 The Ministry of Housing, Communities and Local Government (MHCLG), recently conducted a consultation for a temporary override to allow English local authorities time to adjust their portfolio of investments. The results of the consultation are that the statutory override will apply for five years. The Government will keep the use of the override under review.

12.8 The decision to extend the period of the statutory override to 5 years, instead of 3 years initially proposed in the consultation, is to provide local authorities with the assurance that is needed in their medium term financial planning whilst also allowing time to consider investment strategies. Local authorities are required to disclose the net impact of the unrealised fair value movements in a separate unusable reserve throughout the duration of the override in order for the Government to keep the override under review and to maintain a form of transparency.

12.9 **Changes in risk appetite**

12.10 The 2018 CIPFA Codes and guidance notes have placed enhanced importance on risk management. Where a council changes its risk appetite e.g. for moving surplus cash into or out of certain types of investment funds or other types of investment instruments.

12.11 **IFRS16 (Leases) Accounting Standard**

12.12 IFRS 16 has been delayed until 1 January 2021, whilst additional discussions are held between CIPFA and MHCLG.

12.13 Officers will continue to monitor these discussions and will update their plans accordingly.

12.14 **Revised CIPFA Codes**

12.15 In December 2017 the Chartered Institute of Public Finance and Accountancy (CIPFA) issued a revised Treasury Management Code and Cross Sectoral Guidance Notes and a revised Prudential Code.

12.16 These revisions have particularly focused on non-treasury investments and especially on the purchase of property with a view to generating income. Such purchases could involve undertaking external borrowing to raise the cash to finance these purchases or the use of existing cash balances. Both actions would affect treasury management. As the Localism Act 2011 only gave English authorities a General Power of Competence, these changes in the revised Codes were particularly relevant to the activities of English authorities.

12.17 One recommendation was that local authorities should produce an annual capital strategy, effective from 1st April 2019, to deal with the above issues. It will be for each individual council to decide whether to include their treasury management strategy and annual investment strategy as part of a capital strategy, or to do them separately. However, it was felt that the capital strategy should be a high level corporate document dealing with the key areas of strategic context, corporate priorities, capital investment ambition, available resources, affordability, capacity to deliver, risk appetite, risk management and determining an appropriate split between non-financial and treasury management investments in the context of ensuring the long term financial sustainability of the Council. It should also deal with significant commercial, focused on income generation, investments in appropriate detail so that members can properly assess the particular risks in this area.

12.18 All requirements from the various Code changes were included in the Treasury Management Strategy 2019/20 to 2021/22 that was approved by Council at its meeting on 12th February 2019.

13. **Financial Implications** – are covered in the body of this report.

14. **Legal Implications** - The Council's treasury management activities are regulated by a variety of professional codes, statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity.
- The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (no restrictions were made in 2018/19).
- The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act.
- The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities. The Prudential Code required indicators to be set, some of which are limits, for a minimum of the three forthcoming years.
- The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services.
- Under the Act MHCLG (formerly DCLG) has issued Investment Guidance to structure and regulate the Council's investment activities. Updated Guidance became available on 2nd February 2018 (first published 1st April 2010). The emphasis of the Guidance for treasury management and other financial investments is that local authorities should continue to prioritise security, liquidity and yield in that order of importance.

The Council has complied with all of the above relevant statutory and regulatory requirements that limit the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach.

15. **CORPORATE IMPLICATIONS**

Monitoring Officer commentary – The Monitoring Officer confirms that all relevant legal implications have been taken into account.

S151 Officer commentary - The S151 Officer confirms that all financial implications have been taken into account and that the Treasury Management Outturn Report for 18/19 fully complies with the Treasury Management Strategy 18/19, approved in February 2018.

Risk Implications - The Council considers security, liquidity and yield, in that order, when making investment decisions:

Security – counterparty credit quality was assessed and monitored with reference to credit ratings, credit default swaps, gross domestic product (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 2018/19 was A/A3/A (Fitch/Moody's/Standard and Poors).

Liquidity – the Council maintained a sufficient, though not excessive, level of liquidity during the year using a call account and short-term, fixed-rate, deposits.

Yield – the Council sought to optimise returns commensurate with its objectives of security and liquidity. Short-term money market rates remained at very low levels throughout the year which had a significant impact on investment income.

A high reliance on investment income can place the Council at significant risk of budget variation as interest rates rise and fall, which has an impact upon future Council Tax levels. The Council's Medium Term Financial Strategy addresses this risk and seeks to reduce this reliance over time.

Locking significant investments into long-term fixed-rate deals means the Council has a potential disadvantage in a rising interest market, especially if the interest rate rises above the assumption made when the long-term deal was placed.

To mitigate this, the Council's in-house team predominantly invest up to periods of two months only, hence advantage can be taken of prevailing interest rates upon the investments maturity. This minimises the disadvantage whilst maintaining certainty over the level of future return and stability in planned future Council Tax levels.

The Council will continue to look to diversify its investment portfolio and the 2019/20 Treasury Management Strategy provides for alternative investment funds should the opportunity arise.

Equalities Implications – There are no equalities implications arising as a direct consequence of this report.

Employment Issues - None within the report.

Sustainability Issues - None within the report.

Consultation – The Council is in regular contact with Link Asset Services, the Council's appointed Treasury Management advisor. Conversations, meetings and training have been held during the year involving Link Asset Services and officers.

16. BACKGROUND PAPERS

CIPFA Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes (2017 edition).

CIPFA Treasury Management in the Public Services – Guidance Notes for Local Authorities including Police Authorities and Fire Authorities (2011 & 2017 editions).

CIPFA the Prudential Code for Capital Finance in Local Authorities (2011 & 2017 editions).

Treasury Management Annual Strategy Report 2018-19 and Prudential Indicators 2018-19 to 2020-21.

Performance management information from Link Asset Services, Treasury Solutions.

2018/19 final accounts working papers.

APPENDIX A

1. **PRUDENTIAL AND TREASURY MANAGEMENT INDICATORS AND COMPLIANCE ISSUES**

1.1 The treasury management service is an important part of the overall financial management of the Council's affairs. Whilst the Prudential Indicators consider the affordability and impact of capital expenditure decisions, the treasury management service covers the effective funding of these decisions.

1.2 The 2017 edition of the Prudential Code for Capital Finance in Local Authorities requires that the actual position at year end for designated prudential indicators is reported after the year-end. The table below summarises the prudential indicator performance for 2018/19 for these indicators only.

1.3 The Council at its meeting on 20th February 2018 adopted the following prudential indicators for 2018/19 (Estimate). The full list of Prudential Indicators is set out at Appendix B.

PRUDENTIAL INDICATORS

2017/18 Actual	PRUDENTIAL INDICATOR	2018/19 Estimate	2018/19 Actual
	CAPITAL EXPENDITURE / AFFORDABILITY		
	Capital Expenditure Plans– Prudential Indicator 1		
£000's		**£000's**	**£000's**
48,430	Capital Expenditure	111,120	60,104
48,430	**Total**	**111,120**	**60,104**
	Capital Financing Requirement (CFR) – Prudential Indicator 2		
£000's		**£000's**	**£000's**
57,619	Capital Financing Requirement	111,326	57,628
57,619	**Total**	**111,326**	**57,628**
	Ratio of Net Financing Costs to Net Revenue Stream – Prudential Indicator 3		
%		**%**	**%**
(2.94)	Ratio of Net Financing Costs to Net Revenue Stream	(0.13)	(6.93)
(2.94)	**Total**	**(0.13)**	**(6.93)**
	Borrowing and the Capital Financing Requirement (CFR) – Prudential Indicator 4		
£000's		**£000's**	**£000's**
50,000	External Debt	104,566	102,850

Capital Financing Requirement (CFR)

1.4 The CFR is derived from the Council's balance sheet and measures its underlying need to borrow for a capital purpose. Where capital expenditure is to be financed in future years by charges to revenue as assets are used by the Council, the expenditure results in an increase in the Capital Financing Requirement, a measure of the capital expenditure incurred historically by the Council that has yet to be finalised.

1.5 In accordance with best practice this Council does not associate borrowing with particular items or types of expenditure, in day-to-day cash management no distinction can be made between capital cash and revenue cash. Any external borrowing would arise as a consequence on all financial transactions whereas this measure reflects the Council's underlying need to borrow for a capital purpose only.

Net Borrowing and the CFR

1.6 In order to ensure that borrowing levels are prudent over the medium term the Council's external borrowing, net of investments, must only be for a capital purpose. Net borrowing should not therefore, except in the short term, have exceeded the CFR for 2018/19. Prudential Indicator 5 demonstrates the Council's compliance with this.

TREASURY MANAGEMENT INDICATORS

The Operational Boundary – <u>Prudential Indicator 5</u>

1.7 The Operational Boundary is the expected borrowing position of the Council during the year, and periods where the actual position is either below or over the Operational Boundary is acceptable subject to the Authorised Limit not being exceeded. The Operational Boundary does not allow for additional headroom as is the case with the Authorised Limit. A limit of £129,5m (2017/18: £63.9m) was used for the Operational Boundary. The actual outturn was £104.6m (2017/18: £43.4m) of which £102.9m (2017/18: £40m) was for external borrowing and £1.7m (2017/18: £1.7m) for finance lease liabilities.

The Authorised Limit – <u>Prudential Indicator 6</u>

1.8 The Authorised Limit is the 'Affordable Borrowing Limit' required by S3 of the Local Government Act 2003 irrespective of the Council's indebted status. The limit is the maximum amount of external debt that can be outstanding at any one time during the financial year. The Authorised Limit also provides some headroom for unexpected cash movements. The introduction of International Financial Reporting Standards (IFRS) required finance leases to be included under other long-term liabilities on the balance sheet. A limit of £134.7m (2017/18: £69.1m) was used for the Authorised Limit. The actual outturn was £104,6m (2017/18: £43.4m).

Actual financing costs as a proportion of net revenue stream

1.9 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.

1.10 During the year the Council borrowed £52.9m. Interest payable on external loans during 2018/19 was £2.0m.

Investment Activity

1.11 The purpose of the following indicators is to contain the activity of the treasury management function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates.

1.12 **Maximum principal sums invested > 365 days – <u>Prudential Indicator 7</u>**

Maximum principal sums invested > 365 days			
	2017/18 Actual	**2018/19 Estimate**	**2018/19 Actual**
Principal sums invested > 365 days	£46.2m	£60m	£59.05m

1.13 **Interest rate exposure – <u>Prudential Indicator 8</u>**

Interest rate exposures	**2017/18 Actual**	**2018/19 Estimate**	**2018/19 Actual**
	Upper	**Upper**	**Upper**
Limits on variable interest rates:			
• Debt only	0%	0%	0%
• Investments only	38%	50%	39%
Limits on fixed interest rates:			
• Debt only	100%	100%	100%
• Investments only	62%	100%	61%

1.14 **Maturity structure of fixed interest rate borrowing 2018/19 – <u>Prudential Indicator 9</u>**

	Maturity structure of fixed interest rate borrowing 2018/19			
	2018/19 Estimate		**2018/19 Actual**	
	Lower	**Upper**	**Lower**	**Upper**
Under 12 months	0%	15%	0%	0%
12 months to 2 years	0%	10%	0%	0%
2 years to 5 years	0%	10%	0%	0%
5 years to 10 years	0%	30%	0%	0%
10 years and above	0%	100%	0%	100%

APPENDIX B

THE 9 PRUDENTIAL INDICATORS

The Indicators demonstrate overall control of capital expenditure and that the level of expenditure is sustainable and affordable. They are required by legislation to be set and approved before the start of the year, monitored during the year and reported on at year end.

They address:-

1. Plans for capital expenditure – the projected capital expenditure for each of the next three years and the source of funding.

2. Capital Financing Requirement (CFR) – the anticipated need for borrowing where capital cannot be financed by existing resources.

3. Affordability indicator – the ratio of capital financing costs to the net revenue budget.

4. Comparison of borrowing estimate and capital financing requirement, to confirm that borrowing is intended for capital purposes only.

5. Operational Boundary for external debt – is based on the Council's estimate of most likely - i.e. prudent, but not worst case scenario for external debt.

6. Authorised Limit for external debt – is the maximum amount of debt that the Council can legally owe. The Authorised Limit provides headroom over and above the Operational Boundary for unusual cash movements.

7. To preserve liquidity, the maximum value of investments for more than one year.

8. To assess interest rate exposure, the upper limit on variable and fixed interest rates, in debt and investments.

9. The maturity structure of fixed interest rate borrowing, to regulate the Council's exposure to large repayment requirements.