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| PART B: | RECOMMENDATIONS TO COUNCIL |
| REPORT TO: | POLICY AND RESOURCES COMMITTEE |
| DATE: | 24 JULY 2019 |
| REPORT OF THE: | CHIEF FINANCE OFFICER (s151) – ANTON HODGE |
| TITLE OF REPORT: | TREASURY MANAGEMENT ANNUAL REPORT 2018-19 |
| WARDS AFFECTED: | ALL |

EXECUTIVE SUMMARY

1.0 PURPOSE OF REPORT

1.1 The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2018/19. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

2.0 RECOMMENDATIONS

- 2.1 That Council is recommended to:
- (i) Note the annual treasury management report for 2018/19; and
 - (ii) Approve the actual 2018/19 prudential and treasury indicators in this report.

3.0 REASON FOR RECOMMENDATIONS

3.1 The Council has adopted the Code. A provision of the Code is that an annual review report must be made to the Full Council relating to the treasury activities of the previous year.

4.0 SIGNIFICANT RISKS

4.1 There are significant risks when investing public funds especially with unknown institutions. However, by the adoption of the CIPFA Code and a prudent investment strategy these are minimised. The employment of Treasury Advisors also helps reduce the risk.

5.0 POLICY CONTEXT AND CONSULTATION

- 5.1 The Council has adopted the CIPFA Code of Practice on Treasury Management in Local Authorities and this report complies with the requirements under this code.
- 5.2 The Council uses the services of Link Asset Services – Treasury Solutions (Link) to provide treasury management information and advice.

REPORT

6.0 REPORT DETAILS

6.1 During 2018/19 the minimum reporting requirements were that the full Council should receive the following reports:

- An annual treasury strategy in advance of the year (Council 22 February 2018)
- A mid year (minimum) treasury update report (Audit, Overview & Scrutiny Committee 25 October 2018)
- An annual review following the end of the year describing the activity compared to the strategy (this report).

6.2 The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is therefore 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.

6.3 This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to all the above treasury management reports by the Overview and Scrutiny Committee before they were reported to the full Council.

6.4 This report summarises:

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- Reporting of the required prudential and treasury indicators;
- Summary of interest rate movement in the year;
- Detailed borrowing activity;
- Detailed investment activity.

The Council's Capital Expenditure and Financing 2018/19.

6.5 The Council undertakes capital expenditure on long-term assets. 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.

6.6 The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

| | 2018/19 Actual (£) | 2017/18 Actual (£) |
|----------------------------------|-----------------------|-----------------------|
| Total Capital Expenditure | 842,383 | 852,664 |
| Resourced by: | | |
| Capital receipts | 18,592 | 86,468 |
| Capital grants and contributions | 615,307 | 652,324 |
| Capital reserves | 208,484 | 113,871 |
| External Borrowing | - | - |
| Total | 842,382 | 852,664 |

The Economy and Interest rates

6.7 The Council's treasury advisors Link Asset Services – Treasury Solutions (Link) summarised the key points associated with economic activity in 2018/19 as follows:

- Brexit negotiations have been a focus of much attention during the year;
- UK growth in 2018 was weak initially and then strengthened during the year before falling again in the final quarter;
- As expected the MPC raised Bank Rate from 0.50% to 0.75% on 2 August 2018;
- No further rate rises were expected until uncertainties regarding Brexit were resolved; and
- CPI inflation was on a falling trend throughout the year;

6.8 Deposit rates at the start of 2018/19 have gradually increased, as the rate increases in Q3 17/18 and Q2 18/19 have filtered through into investments placed by the Treasury Fund. As expected, there were no further base rate increases during the final quarter, with the final outturn position at £196k, against a forecast of £168k at Q3.

Overall Treasury Position as at 31 March 2019

6.10 The Council's opening and closing treasury position for the financial year was as follows (excluding finance leases):

| | 31 March 2019 Principal | 31 March 2018 Principal |
|------------------------|-------------------------|-------------------------|
| Total Debt | £1.59m | £1.63m |
| CFR | £1.62m | £1.66m |
| Over/(Under) borrowing | -£0.03m | -£0.03m |
| Total Investments | £22.25m | £19,78m |
| Net Debt | -£22.22m | -£19.75m |

The Strategy for 2018/19

6.11 The Treasury Management Strategy for 2018/19 was approved by members at full Council on 22 February 2018.

6.12 The expectation for interest rates incorporated within the Annual Treasury Management Strategy for 2018/19 was based on officers' views at that time, prepared with assistance from the Council's Treasury Management Advisor (Link Asset Services) and supported by a selection of City forecasts.

6.13 The interest rates for the UK were expected to be as follows:

Bank Base Rate was expected to rise from 0.50% to 0.75%. This increase was pushed back from May to August 2018 due to weak GDP growth. It was not expected that Bank Rate would increase again in 2018/19 as a result of the major uncertainty surrounding Brexit.

PWLB Borrowing rates were forecast to rise gradually throughout the next three years in all periods. Variable and short term rates were expected to be the cheaper form of borrowing over the period.

6.14 Based on the above, the Strategy adopted by the Council for 2018/19 was as follows:

a) Long Term Debt to Finance Capital Expenditure (borrowing strategy 2018/19)

2018/19 was expected to continue as a year of low bank interest rates, extending the current opportunity for the Council to utilise an internal borrowing strategy. Borrowing in advance of need within the constraints of the Prudential Code and approved Prudential Indicators would only be considered in exceptional circumstances.

Consideration would be given to financing capital expenditure by taking borrowing from PWLB/money markets, but the key treasury strategy was to postpone borrowing and maintain an under borrowed position to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

In considering this option however, day to day cash flow constraints and the loss of longer term interest stability would also be taken into account together with the possibility of having to replace the internal borrowing with external borrowing in a subsequent year at higher interest rates.

b) Investment of Surplus cash (investment strategy 2018/19)

The County Council's investment priorities are firstly the security of capital and secondly the liquidity of its investments. The highest return would then be sought provided that proper levels of security and liquidity are achieved. The investment risk appetite of the County Council is low in order to give priority to the security of investments.

The Borrowing Requirement and Debt

6.13 The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR) (excluding borrowing by finance leases).

| | 31 March 2017 Actual | 31 March 2019 Budget | 31 March 2019 Actual |
|-----------|-------------------------|-------------------------|-------------------------|
| Total CFR | £1.659m | £1.624m | £1.624m |

Borrowing Rates in 2018/19

6.14 The movement in relevant UK market interest rates for the year was as follows:

a) For Bank Rate

| | % |
|-------------------------------------|------|
| From 1 April 2018 to 1 August 2018 | 0.50 |
| From 2 August 2018 to 31 March 2019 | 0.75 |

b) For PWLB rates (Inclusive of the 0.20% discount rate)

| Item | Range during Year % | Start of Year % | End of Year % | Average in Year % |
|-------------------------|---------------------|-----------------|---------------|-------------------|
| Fixed Interest Maturity | | | | |
| 1 Year | 1.28 – 1.64 | 1.48 | 1.48 | 1.50 |
| 5 Years | 1.50 – 2.07 | 1.84 | 1.55 | 1.80 |
| 10 Years | 1.80 – 2.50 | 2.22 | 1.85 | 2.19 |
| 25 Years | 2.33 – 2.93 | 2.55 | 2.40 | 2.65 |
| 50 Years | 2.16 – 2.79 | 2.27 | 2.23 | 2.46 |

Borrowing Outturn for 2018/19

6.15 No new borrowing was undertaken during the year and scheduled repayments were made. At the end of the financial year the debt portfolio was as follows:

| Lender | Principal | Type | Interest Rate | Maturity |
|--------|-----------|----------|---------------|----------|
| PWLB | £1.00m | Maturity | 3.69% | 45 years |
| PWLB | £0.59m | EIP | 2.99% | 14 years |

Investment Rates in 2018/19

6.16 Deposit rates continued into the start of 2018/19 at previously depressed levels but then slowly increased after the 2 November.

| Item | Range during Year | Start of Year | End of Year | Average during Year |
|-------------|-------------------|---------------|-------------|---------------------|
| | % | % | % | % |
| 7 day LIBID | 0.35 – 0.59 | 0.36 | 0.57 | 0.51 |
| 1 month | 0.37 – 0.61 | 0.39 | 0.61 | 0.54 |
| 3 month | 0.48 – 0.81 | 0.59 | 0.72 | 0.68 |
| 6 month | 0.59 – 0.92 | 0.70 | 0.83 | 0.79 |
| 1 year | 0.75 – 1.06 | 0.88 | 0.94 | 0.94 |

Investment Outturn for 2018/19

- 6.17 The Council's investment policy is governed by MHCLG guidance, which has been implemented in the Annual Investment Strategy approved by the Council on 22 February 2018. 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 rating outlooks, credit default swaps, bank share prices etc).
- 6.18 The investment activity during the year conformed to the approved strategy and the Council had no liquidity difficulties.
- 6.19 The following table shows the result of the investment strategy undertaken by the Council and the relative performance of the internally managed funds against the 7-day LIBID un-compounded rate benchmark:

| | Average Total Investment (£) | Gross Rate of Return | Net Rate of Return | Benchmark Return |
|---------------------------------|------------------------------|----------------------|--------------------|------------------|
| Internally Managed: | | | | |
| Temporary & On-Call Investments | £6.355m | 0.56% | n/a | n/a |
| Fixed Term Deposits | £18.155m | 0.88% | n/a | 0.51% |

- 6.19 **The interest received by the Council from investments in 2018/19 totalled £196k; this compares to an original estimate of £55k.**
- 6.20 The Council's investment position is organised by the Finance Section in order to ensure adequate liquidity for revenue and capital activities and security of investments. Procedures and controls to achieve these objectives are well established both through Member reporting detailed in the summary, and through officer activity detailed in the Treasury Management Practices. At the beginning and the end of 2018/19 the Council's investments position was as follows:

| | 31 March 2019 (£) | 31 March 2018 (£) |
|--------------------------------|-------------------|-------------------|
| Internally Managed Investments | 22,250,142 | 19,776,864 |

- 6.21 The maturity of the investment portfolio was as follows;

| | 31 March 2019 (£) | 31 March 2018 (£) |
|----------------------------------|-------------------|-------------------|
| On-call Investments | 350,142 | 2,676,864 |
| Fixed Term Deposits: | | |
| Repayable within 1 month | 1,000,000 | 0 |
| Repayable 1 month to 3 months | 6,400,000 | 2,500,000 |
| Repayable 3 months to 6 months | 10,500,000 | 12,600,000 |
| Repayable 6 months to 12 months | 4,000,000 | 2,000,000 |
| Repayable 12 months to 24 months | 0 | 0 |
| Total | 22,250,142 | 19,776,864 |

- 6.22 Investments were placed with the following institutions:

| Type of Institution | 31 March 2018 (£) | 31 March 2018 (£) |
|---------------------|-------------------|-------------------|
| UK Clearing Banks | 4,475,142 | 12,776,864 |
| Foreign Banks | 3,000,000 | 4,000,000 |
| Building Societies | 3,000,000 | 3,000,000 |
| Local Authorities | 11,500,000 | 0 |
| Total | 22,250,142 | 19,776,864 |

Compliance with Treasury Limits

6.23 During the financial year the Council operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Management Strategy Statement (annex B).

7.0 IMPLICATIONS

7.1 The following implications have been identified:

- a) Financial
The results of the investment strategy effect the funding of the capital programme.
- b) Legal
There are no legal implications within this report
- c) Other (Equalities, Staffing, Planning, Health & Safety, Climate Change, Environmental, Crime & Disorder)
There are no additional implications within this report.

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Background Papers: None