ITEM NO	

REPORT TO EXECUTIVE

DATE	**28th November 2018**
PORTFOLIO	**Resources and Performance Management**
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2018/19 Treasury Management Mid-Year Report

PURPOSE

1. To report treasury management activity for the first half year of 2018/19 covering the period 1 April to 30 September 2018.

RECOMMENDATION

2. The Executive is requested to;

   - Note the treasury management activities undertaken during the period 1 April to 30 September 2018, and;

   Recommend that Full Council;

   - Endorse the mid-year update on Treasury Management Strategy for 2018/19 in compliance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management.

REASONS FOR RECOMMENDATION

3. - To inform members of the treasury management activity in the first half of 2018/19 and to fulfil statutory and regulatory requirements.

SUMMARY OF KEY POINTS

4. <u>Background</u>

The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. The first main function of treasury management operations is to ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering maximising investment return.

The second main function of the treasury management service is to ensure the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending commitments. This management of longer term cash may involve arranging long or short term loans, or using cash flow surpluses, and, on occasions, any current debt may be restructured to meet Council risk or cost objectives.

Treasury management is defined as:

> "The management of the Council's borrowing, investments and 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."

The monitoring requirements for treasury were set out in the report which included both the Treasury Management Strategy for 2018/19 and the Prudential and Treasury Indicators for 2018/19 – 2020/21, approved by Full Council on the 21 February 2018.

5.

Introduction

This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017).

The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Strategy which sets out the policies and objectives of the Council's treasury management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
3. Receipt by the Full Council of an annual Treasury Management Strategy - including the Annual Investment Strategy and Minimum Revenue Provision Policy for the year ahead, a **Mid-year Review Report** and an Annual Report (stewardship report) covering activities during the previous year.
4. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is the Scrutiny Committee.

This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the first six months of 2018/19;
- A review of the Treasury Management Strategy and Annual Investment Strategy;
- The Council's capital expenditure, as set out in the Capital Strategy, and prudential indicators;
- A review of the Council's investment portfolio for 2018/19;
- A review of the Council's borrowing strategy for 2018/19;
- A review of any debt rescheduling undertaken during 2018/19;
- A review of compliance with Treasury and Prudential Limits for 2018/19.

6. **Economic Update (Provided by Link Asset Services)**

The first half of 2018/19 has seen UK economic growth post a modest performance, but sufficiently robust for the Monetary Policy Committee, (MPC), to unanimously (9-0) vote to increase Bank Rate on 2 August from 0.5% to 0.75%. Although growth looks as if it will only be modest at around 1.5% in 2018, the Bank of England's August Quarterly Inflation Report forecast that growth will pick up to 1.8% in 2019, albeit there were several caveats – mainly related to whether or not the UK achieves an orderly withdrawal from the European Union in March 2019.

Some MPC members have expressed concerns about a build-up of inflationary pressures, particularly with the pound falling in value again against both the US dollar and the Euro. The Consumer Price Index (CPI) measure of inflation rose unexpectedly from 2.4% in June to 2.7% in August due to increases in volatile components, but is expected to fall back to the 2% inflation target over the next two years given a scenario of minimal increases in Bank Rate. The MPC has indicated Bank Rate would need to be in the region of 1.5% by March 2021 for inflation to stay on track. Financial markets are currently pricing in the next increase in Bank Rate for the second half of 2019.

As for the labour market**,** unemployment has continued at a 43 year low of 4% on the Independent Labour Organisation measure. A combination of job vacancies hitting an all-time high in July, together with negligible growth in total employment numbers, indicates that employers are now having major difficulties filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation picked up to 2.9%, (3 month average regular pay, excluding bonuses) and to a one month figure in July of 3.1%. This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 0.4%, near to the joint high of 0.5% since 2009 (the previous high point was in July 2015.) Given the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. This tends to confirm that the MPC were right to start on a cautious increase in Bank Rate in August as it views wage inflation in excess of 3% as increasing inflationary pressures within the UK economy. However, the MPC will need to tread cautiously before increasing Bank Rate again, especially given all the uncertainties around Brexit.

In the political arena, there is a risk that the current Conservative minority government may be unable to muster a majority in the Commons over Brexit. However, our central position is that Prime Minister May's government will endure, despite various setbacks, along the route to Brexit in March 2019. If, however, the UK faces a general election in the next 12 months, this could result in a potential loosening of monetary policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

7. **Interest Rate Forecast (Provided by Link Asset Services)**

The flow of generally positive economic statistics after the end of the quarter ended 30 June meant that it came as no surprise that the MPC came to a decision on 2 August to make the first increase in Bank Rate above 0.5% since the financial crash, to 0.75%. However, the MPC emphasised again, that future Bank Rate increases would be gradual and would rise to a much lower equilibrium rate, (where monetary policy is neither expansionary or contractionary), than before the crash; indeed they gave a figure for this of around 2.5% in ten years' time but they declined to give a medium term forecast. We

do not think that the MPC will increase Bank Rate in February 2019, ahead of the deadline in March for Brexit. We also feel that the MPC is more likely to wait until August 2019, than May 2019, before the next increase, to be followed by further increases of 0.25% in May and November 2020 to reach 1.5%. However, the cautious pace of even these limited increases is dependent on a reasonably orderly Brexit.

Link Asset Services Interest Rate View											
	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Bank Rate View	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.50%	1.50%
3 Month LIBID	0.75%	0.80%	0.80%	0.90%	1.10%	1.10%	1.20%	1.40%	1.50%	1.60%	1.60%
6 Month LIBID	0.85%	0.90%	0.90%	1.00%	1.20%	1.20%	1.30%	1.50%	1.60%	1.70%	1.70%
12 Month LIBID	1.00%	1.00%	1.00%	1.10%	1.30%	1.30%	1.40%	1.60%	1.70%	1.80%	1.80%
5yr PWLB Rate	2.00%	2.00%	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.60%
10yr PWLB Rate	2.40%	2.50%	2.50%	2.60%	2.70%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%
25yr PWLB Rate	2.80%	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.50%	3.50%
50yr PWLB Rate	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%

8. **Treasury Management Strategy update**

The Treasury Management Strategy (TMS) for 2018/19, which includes the Annual Investment Strategy, was approved by this Council on 21 February 2018. There are no policy changes to the TMS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

9. **The Council's Capital Position**

The table below shows the financing of the Original Capital Budget approved by Full Council on the 21 February 2018 and the latest Revised Capital Budget. The decrease is due to a combination of in year budget monitoring adjustments and reprofiling of capital expenditure into future years.

Capital	2018/19 Original Estimate £'000	2018/19 Revised Estimate £'000
Total Budget	**10,140**	**10,107**
Financed by:		
Capital receipts	2,384	2,687
Capital grants	5,337	3,834
Revenue	828	1,772
Total financing	**8,549**	**8,293**
Borrowing need	**1,591**	**1,814**

10. **Investment Portfolio 2018/19**

Investment rates available in the market have also continued at historically low levels. The average daily level of funds deposited during the financial year to date is £14.7m, compared with £11.4m for the same period in 2017/18. The actual value of funds deposited on the 30 September was £15.844m. These funds have been available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme.

There were 5 investments carried forward from 2017/18 totalling £14.1m, of which £6.1m was with our bank HSBC, £4m was in fixed term deposits with Goldman Sachs, and £4m in a 95 day notice account with Bank of Scotland.

There have been 3 new investments made during the period 1 April to 30 September 2018 totalling £4m, as well as a daily average of £6.7m being invested with HSBC's deposit account, earning between 0.35% and 0.60% interest.

The Council has an approved list of counterparties which governs treasury management investment activity. This list is a restricted list taking into consideration the credit rating of the institution concerned and there are also limits on the amount which can be invested with any particular institution from a particular sector e.g. building society, bank etc. and also any group of institutions within an overall banking group. As part of the daily operations of the treasury management dealings, in consultation with guidance from Link Asset Services and the money market brokers, decisions are taken by the Head of Finance & Property Services, temporarily suspending/revising operations with individual counterparties. The latest deposit counterparties list was approved by the Full Council on 21 February 2018.

The current investment counterparty criteria selection approved in the TMS is meeting the requirement of the treasury management function.

Appendix 1 shows the maximum amount invested with any of the counter parties at any one time during the period 1 April to 30 September 2018. The maximum limit per counterparty is shown in brackets. None of the limits were breached.

Appendix 2 provides Members with an analysis of the Council's total short-term deposits during the period 1 April to 30 September 2018, as well as comparing this to the total deposits placed on a daily basis throughout the 2018/19 financial year.

11. **Property Funds**

The option to invest a maximum of £2m in a Property Fund was approved by the Executive in November 2017. Officers are currently working through the selection process with the councils' treasury management advisors, Link Asset Services.

12. **Borrowing**

Below is a summary of the Councils' external indebtedness, as at 1 April 2018, and as at 30 September 2018.

Borrowing	1 Apr 18 £'000	30 Sept 18 £'000	Change Apr – Sept £'000
Public Works Loan Board	24,087	23,072	(1,015)
Temporary Market Loans	47	10	(37)
Total	**24,134**	**23,082**	**(1,052)**

PWLB Loans – There were two loans of £1m and £15k repaid on 30 September 2018.

Temporary Market Loans – The Edward Stocks Massey Fund withdrew £37k in May 2018.

13. **Debt Rescheduling**

There have been no debt rescheduling opportunities in the current economic climate and consequent structure of interest rates. Therefore, no debt rescheduling was undertaken during the first six months of 2018/19.

14. **Compliance with Treasury & Prudential Limits**

It is a statutory duty for the Council to determine and keep under review its affordable borrowing limits. The Council's approved Treasury and Prudential Indicators (affordability limits) are included in the approved Treasury Management Strategy.

During the financial year to date the Council's treasury management activities operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Management Strategy in compliance with the Council's Treasury Management Practices.

An extract of the Prudential and Treasury Indicators are shown in Appendix 3.

15. **Interest Payable on External Borrowing / Interest Receivable**

Provision is made in the revenue budget to meet the net interest payable on external borrowing. The figure in the original budget for 2018/19 was set at £917,910.

During revenue budget monitoring this budget has been revised down to £868,270 as a result of reducing the budget requirement for PWLB interest paid in the year.

The total interest receivable on temporary deposits for the period 1 April 2018 to 30 September 2018 amounted to £53,189 compared with a revised budget for the year of £69,845 and is therefore forecast to be achieved.

FINANCIAL IMPLICATIONS AND BUDGET PROVISION

16. None arising as a direct result of this report.

POLICY IMPLICATIONS

17. Compliance with the revised CIPFA Code of Practice on Treasury Management.

DETAILS OF CONSULTATION

18. None.

BACKGROUND PAPERS

19. None.

FURTHER INFORMATION
PLEASE CONTACT: **Howard Hamilton-Smith - Finance Manager**