ITEM NO	

REPORT TO EXECUTIVE

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PORTFOLIO	Resources and Performance Management
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Annual Treasury Management Report
Review of 2019/20 Activity

PURPOSE

1. To inform members of the Council's treasury management activity during 2019/20.

RECOMMENDATION

2. That the Executive recommends that Full Council note the annual treasury management activity for the year ended 31 March 2020.

REASONS FOR RECOMMENDATION

3. To comply with the regulations issued under the Local Government Act 2003 to produce an annual treasury management report review of activities and the actual prudential and treasury indicators for 2019/20. 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). Performance against the approved prudential and treasury indicators are shown in Appendix 1.

   During 2019/20 the minimum reporting requirements were that Full Council should receive the following reports:

   - an annual treasury strategy in advance of the year (Full Council 20 February 2019)
   - a mid-year treasury update report (Full Council 18 December 2019)
   - an annual review following the end of the year describing the activity compared to the strategy (this report).

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

It has been a challenging year in terms of returns on investments and this was further impacted in March by COVID-19 and two reductions in the Bank Rate, from 0.75% to 0.10% .

This 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 Scrutiny Committee before they were reported to Full Council. Member training on treasury management issues was undertaken during the year on 10 December 2019 in order to support Members' scrutiny role.

SUMMARY OF KEY POINTS

4. **The Economy and Interest Rates (Provided by Link Asset Services)**
Economic growth in 2019 has been very volatile with quarter 1 unexpectedly strong at 0.5%, to quarter 4 flat at 0.0%. The year 2020 started with optimistic business surveys pointing to an upswing in growth after the ending of political uncertainty as a result of the decisive result of the general election in December settled the Brexit issue. However, the three monthly GDP statistics in January were disappointing, being stuck at 0.0% growth. Since then, the whole world has changed as a result of the coronavirus outbreak. It now looks likely that the closedown of whole sections of the economy will result in a fall in GDP of at least 15% in quarter two. What is uncertain, however, is the extent of the damage that will be done to businesses by the end of the lock down period, when the end of the lock down will occur, whether there could be a second wave of the outbreak, how soon a vaccine will be created and then how quickly it can be administered to the population. This leaves huge uncertainties as to how quickly the economy will recover.

After the Monetary Policy Committee (MPC) raised Bank Rate from 0.5% to 0.75% in August 2018, Brexit uncertainty caused the MPC to do nothing until March 2020; at this point it was abundantly clear that the coronavirus outbreak posed a huge threat to the economy of the UK. Two emergency cuts in Bank Rate from 0.75% occurred in March, first to 0.25% and then to 0.10%. These cuts were accompanied by an increase in quantitative easing (QE), essentially the purchases of gilts (mainly) by the Bank of England of £200bn. The Government and the Bank were also very concerned to stop people losing their jobs during this lock down period. Accordingly, the Government introduced various schemes to subsidise both employed and self-employed jobs for three months while the country was locked down. It also put in place a raft of other measures to help businesses access loans from their banks, (with the Government providing guarantees to the banks against losses), to tide them over the lock down period when some firms may have little or no income. This leaves open a question as to whether some firms will be solvent, even if they take out such loans, and some may also choose to close as there is, and will be, insufficient demand for their services.

Inflation has posed little concern for the MPC during the last year, being mainly between 1.5 – 2.0%. It is also not going to be an issue for the near future as the world economy will be heading into a recession which is already causing a glut in the supply of oil which has fallen sharply in price. Other prices will also be under downward pressure while wage inflation has also been on a downward path over the last half year and is likely to continue that trend in the current environment. While inflation could even turn negative in the Eurozone, this is currently not likely in the UK.

5. The Strategy for 2019/20

5.1 Investment Strategy and control of interest rate risk

Investment returns remained low during 2019/20. The expectation for interest rates within the treasury management strategy for 2019/20 was that Bank Rate would stay at 0.75% during 2019/20 as it was not expected that the MPC would be able to deliver on an increase in Bank Rate until the Brexit issue was finally settled. However, there was an expectation that Bank Rate would rise after that issue was settled, but would only rise to 1.0% during 2020. Rising concerns over the possibility that the UK could leave the EU at the end of October 2019 caused longer term investment rates to be on a falling trend for most of April to September. They then rose after the end of October deadline was rejected by the Commons but fell back again in January before recovering again after the 31 January departure of the UK from the EU.

When the coronavirus outbreak hit the UK in February/March, rates initially plunged but then rose sharply back up again due to a shortage of liquidity in financial markets. As longer term rates were significantly higher than shorter term rates during the year, value was therefore sought by placing longer term investments where cash balances were sufficient to allow this.

5.2 Borrowing Strategy and control of interest rate risk

A policy of avoiding new borrowing by running down spare cash balances has previously been adopted and has served well over the last few years. However, this has been kept under review to avoid incurring higher borrowing costs in the future when this authority may not be able to avoid new borrowing to finance capital expenditure.

During 2019-20 the Council increased it’s borrowing to fully fund the CFR (the Capital Finance Requirement). This strategy was prudent as borrowing rates fell to historically low levels during the year.

6. The Borrowing Requirement and Debt

The Council’s underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR). The table below shows the Council’s CFR for 2019/20.

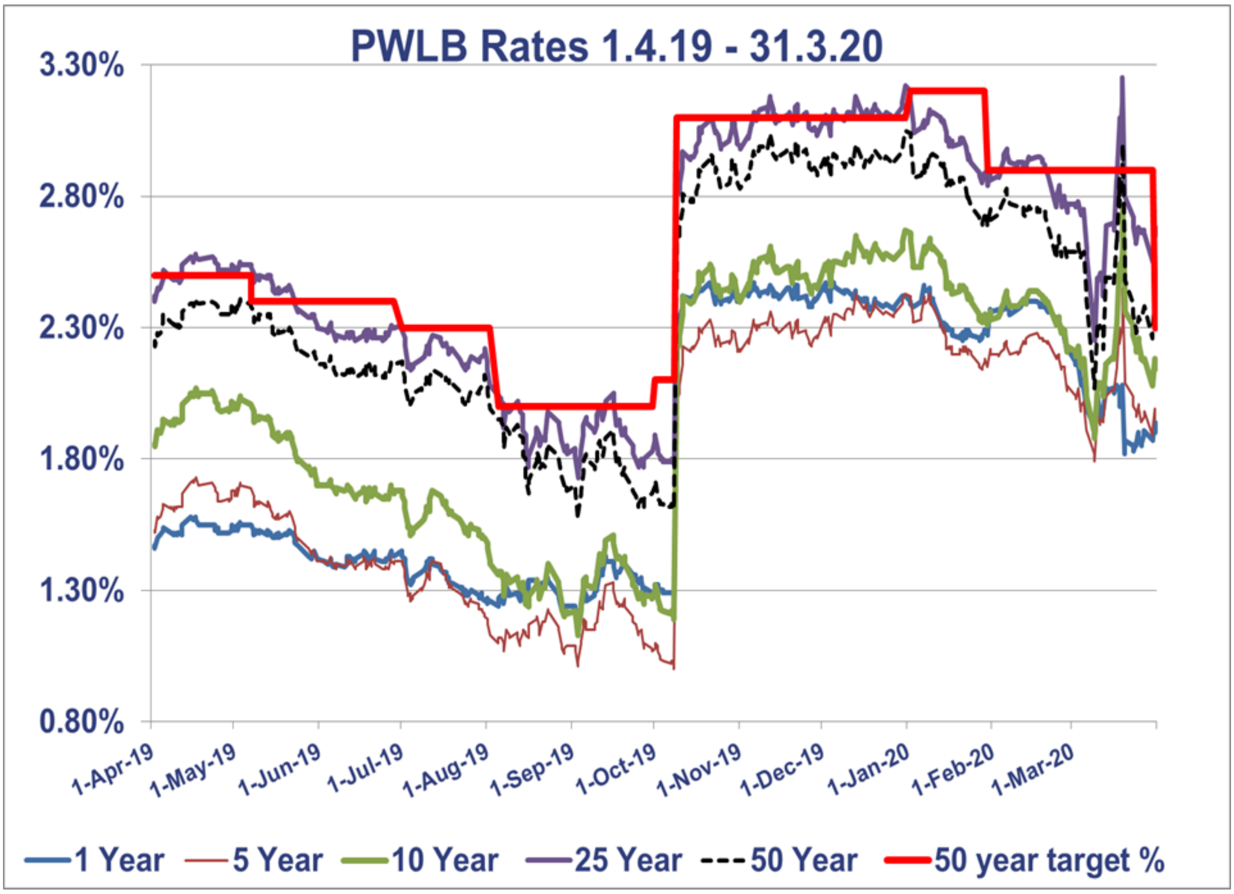
£m	31 March 2019 Actual	31 March 2020 Budget	31 March 2020 Actual
CFR General Fund	30.5	36.8	37.7

7. **Borrowing Rates in 2019/20**

PWLB rates are based on, and are determined by, gilt (UK Government bonds) yields through H.M.Treasury determining a specified margin to add to gilt yields. There was much speculation during the second half of 2019 that bond markets were in a bubble which was driving bond prices up and yields down to historically very low levels.

HM Treasury imposed a change in the margins over gilt yields for PWLB rates in 2019-20 without any prior warning on 9 October 2019, adding an additional 1% margin over gilts to all PWLB rates.

The graph for PWLB rates show, for a selection of maturity periods, the average borrowing rates, the high and low points in rates, spreads and individual rates at the start and the end of the financial year.



8. **Borrowing Outturn for 2019/20**

Borrowing – The following PWLB loans were taken during the year to fund the net unfinanced capital expenditure and loans that have matured and been repaid in year.

Date	Lender	Principal	Type	Interest Rate	Duration
20/5/19	PWLB	£5m	Maturity	2.28%	50 years
05/7/19	PWLB	£1m	Maturity	2.03%	48 years
05/7/19	PWLB	£2m	Maturity	2.03%	49 years
06/8/19	PWLB	£2m	Maturity	1.99%	46 years
06/8/19	PWLB	£1m	Maturity	1.99%	47 years
20/8/19	PWLB	£1m	Maturity	1.68%	45 years
13/12/19	PWLB	£1m	Maturity	2.95%	43 years
10/3/20	PWLB	£1m	Maturity	2.41%	50 years
11/3/20	PWLB	£2m	Maturity	2.07%	49 years

This compares to a budget assumption of borrowing at an interest rate between 2.8 and 3%.

Rescheduling – No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Repayments – The following PWLB loan was repaid during the year, as scheduled:

Date	Lender	Principal	Balance at Repayment	Type	Interest Rate	Duration
30/9/19	PWLB	£1.4m	£1.4m	Maturity	4.9%	16 years

9. **Investment Rates in 2019/20**

The Council operates a deposit account with it's bank, HSBC, which pays an interest rate of 0.15% below Bank Rate. On 10 March 2020 Bank Rate was cut from 0.75% to 0.25% in response to the coronavirus outbreak. The Bank Rate was further cut to 0.10% on 19 March 2020. The interest rate on the Deposit account was therefore reduced from 0.6% to nil by the end of the year. There was an average daily total of £10.38m being invested within the HSBC "sweep" deposit account, which earned an average of 0.57% in 2019/20.

10. **Investment Outturn for 2019/20**

Investment Policy – the Council's investment policy is governed by MHCLG investment guidance, which has been implemented in the annual investment strategy approved by Full Council on 20 February 2019. 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. This guidance is enhanced by advice from Link Asset Services.

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Investments held by the Council - the Council maintained a daily average balance of £19.7m of internally managed funds during 2019/20. These investments earned an average rate of return of 0.76% which exceeded the target of base rate 0.75% minus 0.2%.

There were a total of 10 market investments made during the financial year, totalling £16m. This includes two investments made with Bank of Scotland that were transferred in year from notice accounts to fixed longer term deposits, in order to secure a higher return against the risk of interest rates falling.The table below shows the amount deposited, and the rate of return against the market benchmark.

Counterparties	Date of Investment	Investment Made £m	Return	Benchmark
Bank of Scotland (95 Day Notice)	20/05/2019	1.0	1.1%	0.634%
Bank of Scotland (32 Day Notice)	09/07/2019	1.0	0.95%	0.557%
Bank of Scotland (12 month fixed)	09/07/2019	2.0	1.25%	0.798%
Bank of Scotland (12 month Fixed – transferred from notice accounts above)	16/08/2019	2.0	1.1%	0.798%
Santander (3 month Term Deposit)	09/08/2019	2.0	0.9%	0.634%
Santander (6 month Term Deposit)	09/08/2019	2.0	1.0%	0.705%
HSBC (31 Day Notice)	29/07/2019	1.0	0.9%	0.557%
HSBC (31 Day Notice)	17/09/2019	1.0	0.9%	0.557%
HSBC (31 Day Notice)	12/11/2019	2.0	0.9%	0.557%
Suffolk County Council	27/03/2020	2.0	1.1%	0.634%

All investments were for one year or under.

The table below shows the maximum amount invested with any of the counterparties at any one time during the period April 2019 to the end of March 2020 against the maximum limits approved in the 2019/20 Treasury Management Strategy.

Counterparties	Maximum Limits £m	Highest level of Investment 2019/20 (£m)
HSBC	25.0	19.8
Bank of Scotland	4.0	4.0
Suffolk County Council	2.0	2.0
Santander UK plc	4.0	4.0
Goldman Sachs	4.0	1.0

11. **Interest payable on External Borrowing / Interest Receivable on Investments**
The revised budget for the PWLB interest payable on external borrowing for 2019/20 was set at £987,328.

The outturn position was £1,073,568 due to increased borrowing activity during the year to fund the Council's CFR whilst taking advantage of historically low PWLB interest rates.

The total interest receivable on temporary investments in 2019/20 amounted to £133,823 compared with a budget for the year of £69,845, the difference of £63,978 being due to careful and pro-active management of the council's cash balances.

12. **Property Fund Investments, costs & dividends received**
The Council continues to invest £2m in property funds with CCLA and Hermes. Dividends receivable amounted to £68,169 compared to a budget of £70,000.

The aim of the Property Fund investments are to provide high levels of income and long-term capital appreciation. Significant uncertainty remains on the full impact of the Coronavirus pandemic on the property sector with early evidence suggesting that the retail and leisure sectors are those hardest hit.

It is expected that pressures will ease as the economy slowly returns to normal but it is likely to be several months before the full implications are understood. The Council will seek compensation from Central Governemnt for any financial lossess incurred on the Property Funds.

Valuations are being reported on the basis of material value uncertainty (issued without expected confidence in their accuracy) and need to be kept under frequent review. As a consequence property funds have temporarily suspended trading. This is because funds are unable to provide a firm valuation in the circumstances, and cannot therefore meet the requirement to ensure that investors are treated equally when selling or purchasing shares. This will be ongoing until clarity is restored.

Looking forward, there is expected to be a period of economic recovery next year and for this to be reflected in positive returns from the sector; the recession has been a shock to values, but it should be a passing one.

FINANCIAL IMPLICATIONS AND BUDGET PROVISION

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

POLICY IMPLICATIONS

14. All transactions are in accordance with the Council's approved Treasury Policy Statement

DETAILS OF CONSULTATION

15. None

BACKGROUND PAPERS

16. Treasury Management Strategy Report & Prudential Indicators Report for 2019/20.

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