TRAFFORD COUNCIL

Report to: **Accounts & Audit Committee – 31 October 2018**
Executive – 26 November 2018

Report for: **Information**

Report of: **The Executive Member for Finance and the Corporate Director of Finance and Systems**

Report Title

Treasury Management 2018-19 Mid-Year Performance Report

Summary

This report gives Members a summarised account of the Treasury Management activities undertaken for the first half of the year together with an update of the world economic situation.

Debt Activity:-

- Net debt interest costs are currently forecasted to be £5.4m for the year and are contained within the current MTFP,
- At 30 September the Council's external debt was £163.6m.

Investment Activity:-

- The annualised investment interest to be generated is forecasted to be in line with budget of £(0.7)m,
- Rate of Return achieved during the period April to September 2018 was;
  i. short term investments 0.72%, or 0.28% £(113)k above the comparable performance indicator of average 7-day **L**ondon **I**nterbank **BID** interest rate of 0.44% and
  ii. long term investments 4.90%,
- At 30 September the value of Council's investments was £80.0m.

Prudential Indicators:-

- During the first half of 2018/19 the Council complied with its legislative and regulatory requirements, including compliance with all treasury management prudential indicators.

Recommendations

That the Accounts & Audit Committee & Executive be requested to:

1. Note the Treasury Management activities undertaken in the first half of 2018/19.

Contact person for background papers and further information:

Name: Graham Perkins
Extension: 4017 Background papers: None

Relationship to Policy Framework/Corporate Priorities	Value for Money
Financial	The projected level of the Council’s investment and debt net interest for 2018/19 are currently forecasted to be in line with budget of £(0.7)m & £5.4m respectively.
Legal Implications:	All actions undertaken during this period were in accordance with legislation, MHCLG Guidance, CIPFA Prudential Code and CIPFA Treasury Management Code of Practice.
Equality/Diversity Implications	Not applicable
Sustainability Implications	Not applicable
Staffing/E-Government/Asset Management Implications	Not applicable
Risk Management Implications	The monitoring and control of risk underpins all treasury management activities and these factors have been incorporated into the treasury management systems and procedures which are independently tested on a regular basis. The Council’s in-house treasury management team continually monitor interest forecasts and actual market interest rate movements to ensure that any exposure to adverse fluctuations in interest rates are minimised and security of capital sums are maintained at all times.
Health and Safety Implications	Not applicable

1. BACKGROUND

1.1 This report has been issued 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:

- Receipt by the Council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report, covering activities during the previous year.
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
- 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.
- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body and this has been delegated to the Accounts and Audit committee.

1.2 This mid-year report highlights the treasury management activities undertaken during the first half year of 2018/19 as follows;

- Economic Update (section 2)
- Treasury Position (section 3)
- Debt Activity (section 4)
- Investment Activity (section 5)
- Risk Benchmarking (section 6)
- Prudential and Performance Indicators (section 7)
- Other Activity Update (section 8)
- Recommendations (section 9)

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

1.4 Another main function of the treasury management service is the funding of the Council's capital programme. This function highlights any potential borrowing requirement which may involve arranging long or short term loans, or using longer term cash flow surpluses. In addition periodically when the opportunities arise, any debt previously drawn may be restructured to meet Council risk or cost objectives.

2. ECONOMIC UPDATE

2.1 During the first half of 2018/19, the main economic headlines are outlined below and a forecast of the main indicators for 2019 is provided at Appendix B for reference:

UK

- Gross Domestic Product (GDP) for the first quarter of 2018 was +0.2% (1.2% y/y) however due to the hot weather and World Cup "feel good" factor the second quarter came in stronger at 0.4% (1.3% y/y). For 2018 it is currently forecasted that growth will be 1.5%.
- The Monetary Policy Committee (MPC) at its August meeting increased bank rate from 0.50% to 0.75%, the highest it has been since March 2009.
- Consumer Price Index (CPI) was 2.7% in August which is 0.7% above the Government's target of 2.0%.
- Unemployment continues to fall recording a level of 4.0% for the 2nd quarter of 2018, the lowest level it has been since the winter of 1975.
- Uncertainty around Brexit negotiations remains making it difficult to be confident about how the forthcoming year will perform.

U.S.

- The American economy continues to record strong growth with 2.2% (2.6% y/y) for quarter 1 and 4.2% (2.9% y/y) for quarter 2.
- The Federal Bank (Fed) has increased rates twice in 2018 to 2.0% with a further 2 more increases forecasted this year as a result of accelerated growth and rapid job creation.
- Unemployment in the US continues to fall and the latest figures show this to be 3.9%.
- CPI fell by 0.2% in August 2018 to 2.7%.

Eurozone

- European Central Bank (ECB) has maintained the main refinancing rate at 0% with little prospect of any upswing in rates in the near future.
- GDP in quarters 1 and 2 were identical at 0.4% and this as at the end of quarter 2 equates to annual growth of (2.2% y/y).
- CPI was recorded at 2.0% in August, the ECB target rate.
- The 3 month unemployment rate continues its downward trend falling to 8.2% for the period ending July.

Other Countries

- As a result of improving markets Japan's economy recovered strongly in the second quarter of 2018 following the contraction in the previous quarter and consumer spending, however tensions between the US and China could be a cause for concern.
- China's economic growth eased further in July on the back of the prolonged trade war with the U.S. In addition to this the leadership vowed to adopt a more active fiscal policy to bolster the economy.

2.2 The Council's treasury management advisors Link Asset Services, provide interest rate forecasts periodically through-out the year and the table below outlines the latest **average** forecasted rates, as issued in August 2018, for the periods stated:

	2018-19 Original Forecast %	2018-19 Revised Forecast %	2019-20 Revised Forecast %	2020-21 Revised Forecast %
Bank Rate	0.58	0.67	0.90	1.30
Investment Rates 3 month 1 Year	 0.50 0.90	 0.72 0.95	 1.00 1.39	 1.46 1.66
PWLB Loan Rates 5 Year 25 Year	 1.50 3.00	 1.94 2.77	 2.22 3.13	 2.45 3.39

2.3 Previously market analysts were predicting that the Monetary Policy Committee (MPC) wouldn't start increasing the Bank of England's bank rate until December 2018. At its meeting on the 2 August 2018 however, the MPC raised bank rate from 0.50% to 0.75%. This increase was the second in over 10 years and was responding to the positive level of economic statistics released since the end of the first quarter of 2018.

2.4 The MPC also stated at its August meeting that any future increases would be gradual with rates peaking at 2.50% in 10 years' time. With regards to gilt yields and PWLB rates, these are set to rise from their current levels albeit slowly and gently.

2.5 The above interest rate forecasts shown at paragraph 2.2 are based on an assumption that sufficient progress will be made concerning Brexit which benefits both the EU and UK. If however no agreement is reached then forecasters predict that both the Bank rate and PWLB rates will be subject to downward movements in order to avoid any potential recessionary effects which may arise as a result.

2.6 To reduce any risk aspects arising from this situation the Council will continue its policy to take a cautious approach when undertaking money market transactions.

3. TREASURY POSITION

3.1 The Council's investment and debt positions at the beginning and midway through the current financial year are listed in the table shown at paragraph 3.2 below for reference.

3.2 It is important to note that when referring to this information, that the levels of investments fluctuate daily as a result of timing issues from monies being received ahead of spend requirement and are therefore are only available on a temporary basis.

	31 March 2018		30 September 2018	
	Principal **£m**	**Average Interest Rate %**	**Principal** **£m**	**Average Interest Rate %**
DEBT				
Short term (payable before 31.03.19)				
PWLB	2.8	5.83	2.7	5.50
Market	0.0	0.00	0.0	0.00
Government Loans - Salix	1.4	0.00	0.7	0.00
Sub-total	4.2	3.89	3.4	4.38
Long term (payable after 31.03.19)				
PWLB	100.6	3.62	100.6	3.62
Market	56.0	5.50	56.0	5.52
Government Loans - Salix	3.6	0.00	3.6	0.00
Sub-total	160.2	4.21	160.2	4.10
Total debt	**164.4**	**4.19**	**163.6**	**4.21**
INVESTMENTS				
- Instant access	30.3	0.48	19.5	0.70
- Call accounts	7.2	0.57	7.8	0.80
- Term deposit	30.7	0.78	47.7	0.93
- Long term - CCLA	5.0	4.87	5.0	4.90
Total Investments	**73.2**	**0.92**	**80.0**	**1.11**

4. DEBT ACTIVITY

4.1 The Council’s under borrowed position as at 31 March 2018, was £30.7m due to the total Capital Financing Requirement (CFR), the underlying need to borrow for capital purposes, of £195.1m being higher than the actual level of external debt of £164.4m.

4.2 This under borrowed position reflects previous years decisions to apply its own funds (cash supporting reserves & balances) to fund the capital borrowing requirement instead of taking out any new loans. This approach, which continues to be widely adopted by Councils, reflects the current high “cost of carry” situation i.e. the difference between long-term debt interest rates and short-term investment interest rates.

4.3 In response to the Council’s overall financial position and the underlying need to borrow for capital purposes, particularly with regards to funding the commercial investment programme, new external borrowing will be required to be taken. The loan servicing costs associated with new borrowing will be met from either an existing revenue provision within the Medium Term Financial Plan or from applying a proportion of the investment returns generated from the commercial investment programme. All new borrowing which is to undertaken will be done so in conjunction with the information obtained from the Council’s advisors Link Asset Services.

4.4 Prior to the completion of the acquisition of a commercial property, a number of due diligence exercises are carried out ensuring that the Council only completes on worthwhile properties. It is acknowledged however that as a result of potential future events beyond the Council's control, a possible risk arising from tenant default may exist. In order to overcome the effect that this would have on the Council's resources, a new risk reserve has been created which will be applied to this situation.

4.5 During the first half of 2018/19, no new long term loans were taken and the table below highlights the level of debt transactions which occurred during the first half of 2018/19:

Loans	Balance 31 March 2018 £m	Borrowed £m	Debt Repaid £m	Balance 30 September 2018 £m
Short Term	4.2	0.0	0.8	3.4
Long Term	160.2	0.0	0.0	160.2
Total	**164.4**	**0.0**	**0.8**	**163.6**

4.6 The Council currently has 23 loans in total with only 1 of these being subject to quarterly interest rate fixings using a recognised market indicator.

4.7 As a consequence of low interest rates, debt rescheduling opportunities continue to be expensive to complete due to high breakage (premium) costs which would be incurred. During the first half of the year no debt restructuring was undertaken however the situation will continue to be monitored.

5. INVESTMENT ACTIVITY

5.1 In compliance with the Council's Annual Investment Strategy, approved by Council in February 2018, the priorities when placing any temporary surplus funds continues to be that as adopted in previous years of security of capital, liquidity and finally obtaining an appropriate level of return.

5.2 The table below highlights the level of investment transactions carried out during the first half of 2018/19;

Investments	31 March 2018 £m	Made £m	Repaid £m	30 September 2018 £m
Instant access	30.3	180.1	190.9	19.5
Call accounts	7.2	0.6	0.0	7.8
Term deposit	30.7	21.0	4.0	47.7
Long term – CCLA*	5.0	0.0	0.0	5.0
Total	**73.2**	**201.7**	**194.9**	**80.0**

* reflects movement in valuation of the CCLA Property Fund investment.

5.3 The £6.8m upward movement in short-term investments from 31 March 2018 to 30 September 2018 reflects the day to day cash flow movements and monies received ahead of spend.

5.4 All investments placed with any of the Council's approved institutions and which matured during the first half of the financial year, were repaid on time without any difficulties and the list of institutions in which the Council invests continues to be kept under review.

5.5 The movement in the Council's temporary investments as at 31 March 2018 compared to 30 September 2018 is shown below for reference:

Sector	31 March 2018 £m	30 September 2018 £m
UK Banks	31.4	39.0
UK Building Societies	0.0	0.0
Money Market Funds	30.3	19.5
Non UK Banks	2.5	13.5
Local Authority	4.0	3.0
Other - CCLA	5.0	5.0
Total	**73.2**	**80.0**

The maturity structure of the investment portfolio was as follows:

Period	31 March 2018 £m	30 September 2018 £m
Instant Access	30.3	19.5
Up to 3 Months	13.0	14.8
3 to 6 Months	10.9	33.8
6 to 9 Months	2.0	2.9
9 to 12 months	9.5	4.0
Over 1 year	7.5	5.0
Total	**73.2**	**80.0**

5.6 During the first half of the year, a total of 81 short term temporary investments were undertaken by the Council's in-house treasury management team in an environment of slowly increasing but still low interest rates. The table below highlights the results of these activities and this clearly illustrates the Council outperforming the 7day LIBID benchmark, a recognised market performance indicator, by 0.28% on its short term investments whilst ensuring that all risk was kept to a minimum during this period.

Average level of Investments (ex CCLA) 1 April to 30 Sept £m	Average interest rate earned %	Average 7 day LIBID rate %	Additional interest earned against 7 day LIBID £k
79.0	0.72	0.44	(113)

5.7 In September 2015, the Council invested £5m in the Local Authority Property Investment fund, managed by the Church Commissioners Local Authority, (CCLA), and this enabled 1,643,872 units to be purchased in the fund. This fund is only accessible to Local Authorities and its objective is to generate long-term growth in the amount originally invested whilst generating returns in the form of annual dividends by investing in commercial property throughout the UK.

5.8 By the very nature of this type of investment and to enable a satisfactory rate of return to be achieved in the form of capital growth and annual revenue returns, it is expected that funds will be held in this account for a minimum period of 5 years.

5.9 At 31 March 2018 the Council's investment was worth £4.96m and this has now risen to £4.99m as at 30 September 2018. Based on current property growth forecasts there are no concerns on the security and liquidity of this investment, which remains within the limits approved.

5.10 With regards to the level of dividends received, these continue to be strong as a result of the high rental returns being achieved. For reference the annualised level of return generated for the first half of 2018/19 was 4.90% gross of fees compared to 5.27% for the same period in 2017/18. It is anticipated that the return for the remainder of the year will be in line with that achieved for the first half of the year.

5.11 The level of budgeted investment interest forecasted to be generated from all of the Council's investments during 2018/19 was set at £(0.7)m and currently it is forecasted that this will be achieved.

5.12 As outlined at Section 2 above, worldwide events together with the uncertainty surrounding Brexit continue to affect money markets and the potential for earning a respectable level of interest whilst ensuring the Council's risk exposure is kept to a minimum, remains a challenge. In order to maintain risk to a minimum, funds will continue to be placed in low risk counterparties with returns set to reflect this strategy.

5.13 Appendix A details the Council's investments, as at 30 September 2018.

6. RISK BENCHMARKING

6.1 In accordance with the Code and MHCLG Investment Guidance, appropriate security and liquidity benchmarks are used by the in-house treasury management team to monitor the current and future potential risk conditions enabling any corrective action to the strategy to be applied if required.

6.2 These benchmarks are simple guides to maximum risk (not limits) and so may be breached from time to time, depending on movements in interest rates and counterparty criteria.

6.3 During the first half of 2018/19 it can be reported that no benchmarks, which were set in the Strategy report in February 2018, were breached as shown from the table below;

Indicator	Target	Actual
Security – potential default rate of the Council's investment portfolio based on rates issued by the 3 main credit rating agencies.	Max 0.07%	Max 0.02%
Liquidity – investments available within 1 week notice	£10m min.	Achieved
Liquidity – Weighted Average Life of investments (ex CCLA Property Fund)	6 months	This was not breached and as at 30 September was 3.8 months.

Indicator	Target	Actual
Yield – Investment interest return to exceed 7 day **L**ondon **I**nterbank **BID** rate	0.44% (Avg. 7 day LIBID)	0.96% (All Investments)
Origin of investments placed - maximum investments to be directly placed with non-UK counterparties.	UK institutions 100% Non UK institutions 40%	Achieved

7. PRUDENTIAL AND PERFORMANCE INDICATORS

7.1 In accordance with MHCLG Guidance and the Code, a number of prudential indicators are in place ensuring that the Council's capital expenditure plans and borrowing remain robust, prudent and sustainable.

7.2 These indicators which originally approved by Council in February 2018 were subsequently revised and approved by Council at the July 2018 meeting.

7.3 All prudential indicators are monitored on a monthly basis and during the first half of 2018/19 it can be reported that no breaches occurred.

7.4 The Council's Audit & Assurance Service, as part of their 2018/19 audit plan, undertook a review of the treasury management process & activities undertaken in 2017/18. The objective of the review was to provide assurance on the operation of the key controls within the treasury management system. For the 12th year in succession a report was issued stating that the in-house treasury management team offered a High Level of Assurance (very good) and there were no recommendations required to be implemented.

8. OTHER ACTIVITY UPDATE

8.1 The main purpose of this report is to inform Members of the activities undertaken during 1 April 2018 to 30 September 2018 however in addition to that activities outlined above the following events have also occurred;

- Local Authority Mortgage Scheme (LAMS) - the Council participated in the national Local Authority Mortgage Scheme with Lloyds bank placing a total of £3m in 2 separate tranches (£2m at 4.41% and £1m at 2.7%). I can confirm that all funds placed in this scheme have been repaid back to the Council. Spend incurred under this scheme is deemed to be capital expenditure being classified as a service investment and so does not form part of treasury management activities or reports.
- Member Training - this was provided by the Council's advisors Link Asset Services and internal staff to Members of both the Accounts and Audit Committee and Executive on 16 October 2018. The purpose of this training was to support Members in being able to fulfil their responsibilities in accordance with the Code of Practice.

9. RECOMMENDATIONS

9.1 That the Accounts & Audit Committee & Executive be requested to;

- Note the Treasury Management activities undertaken in the first half of 2018/19.

Other Options

This report has been produced in order to comply with Financial Regulations and relevant legislation and provides an overview of transactions undertaken during the first half of 2018/19.

Consultation

Information for the period 1 April 2018 to 30 September 2018 was obtained from Link Asset Services, the Council's external consultants.

Reasons for Recommendation

The report has been produced in order to meet the requirements of the Council's Financial Procedure Rules which incorporate the requirements of both the CIPFA Prudential Code for Capital Finance and the CIPFA Code of Practice on Treasury Management.

Finance Officer Clearance **…GB…….**

Legal Officer Clearance **…DS ……..**

DIRECTOR'S Signature 

APPENDIX A

Breakdown of Investments as at 30 September 2018

Counterparty	(31 March 2018) £000	(30 September 2018) £000
Instant Access (Money Market Funds)		
Amundi	16,200	11,500
Federated Investors	7,320	6,050
Invesco Aim	260	140
Legal & General	200	1,400
Standard Life	6,300	400
Sub-total	*30,280*	*19,490*
Call accounts		
Barclays Bank	5,000	5,000
Santander UK Bank	4,200	4,800
Sub-total	*9,200*	*9,800*
Term Deposit		
Birmingham City Council	0	3,000
Close Brothers Bank	5,500	7,500
Commonwealth Bank of Australia	0	2,000
Development Bank of Singapore	0	9,000
Goldman Sachs Bank	4,500	7,000
Lloyds Bank	12,270	14,670
National Bank of Abu Dhabi	2,500	2,500
Plymouth City Council	2,000	0
Thurrock Council	2,000	0
Sub-total	*28,770*	*45,670*
Long term deposit		
Church Commissioners Local Authority	4,964	4,992
Sub-total	*4,964*	*4,992*
Total UK	**73,214**	**79,952**

The above table shows the level of investments placed at 30 September 2018 and 31 March 2018, the last time Members were provided with this information.

APPENDIX B

Major Economic Forecasts for Calendar Year 2019

Location	Gross Domestic Product	Unemployment Rate	Consumer Price Index	Bank Rate
UK	1.3%	4.6%	2.2%	1.00%
Euro Area	2.1%	7.8%	1.8%	0.05%
USA	2.8%	3.6%	2.3%	2.75%
China	6.4%	n/a	2.0%	4.50%

Source of information OECD % Trading Economics