NORTH WEST LEICESTERSHIRE DISTRICT COUNCIL

CABINET – TUESDAY, 18 JUNE 2019

Title of Report	**TREASURY MANAGEMENT STEWARDSHIP REPORT FOR 2018/19**
Key Decision	a) Financial No b) Community No
Contacts	Councillor Nick Rushton 01530 412059 nicholas.rushton@nwleicestershire.gov.uk Strategic Director of Housing and Customer Services 01530 454819 Glyn.jones@nwleicestershire.gov.uk Head of Finance / S151 Officer 01530 454707 tracy.bingham@nwleicestershire.gov.uk
Purpose of Report	To inform Members of the Council's Treasury Management activity undertaken for the financial year 2018/19.
Reason for Decision	These are statutory requirements
Council Priorities	Value for Money
Implications:	
Financial/Staff	Interest earned on balances and interest paid on external debt, impact on the resources available to the Council.
Health & Safety	Not applicable
Risk Management	Borrowing and investment both carry an element of risk. This risk is mitigated through the adoption of the Treasury and Investment Strategies, compliance with the CIPFA code of Treasury Management and the retention of Treasury Management Advisors (Arlingclose) to proffer expert advice.
Equalities Impact Screening	Not Applicable
Human Rights	Not Applicable
Transformational Government	Not Applicable
Comments of Head of Paid Service	Report is satisfactory
Comments of Section 151 Officer	Report is satisfactory
Comments of Monitoring Officer	Report is satisfactory
Consultees	None

Background Papers	Capital Strategy 2018/19 – Council 27 February 2018 Treasury Management Strategy Statement 2018/19 – Council 27 February 2018 Treasury Management Activity Report April 2018 to February 2019 – Audit and Governance 20 March 2019 Investment Strategy – Service and Commercial 2019/20 – Council 26 February 2019
Recommendations	**THAT MEMBERS NOTE THE REPORT.**

1.0 BACKGROUND

1.1 Treasury Management activity is underpinned by CIPFA's Code of Practice on Treasury Management ("the code"), which requires local authorities to produce Prudential Indicators and a Treasury Management Strategy Statement annually on the likely financing and Investment activity.

1.2 This report fulfils the council's legal obligation under the Local Government Act 2003, to have regard to both the CIPFA Code and the MHCLG Investment Guidance

1.3 In 2018/19, council approved its Capital Strategy (included in the Budget and Council Tax report) and Treasury Management Strategy Statement, including the Borrowing Strategy, Debt Rescheduling Strategy, Annual Investment Policy and Strategy, Interest Apportionment Policy, Prudential Indicators and Annual Minimum Revenue Position Statement in its meeting on 27 February 2018.

1.4 Investing or borrowing activities expose the council to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risks are therefore central to the council's treasury management strategy.

2.0 THE U.K. ECONOMY AND OTHER FACTORS.

2.1 An economic update and interest rate forecast has been provided by our Treasury Advisers (Arlingclose Ltd) and summarised below. A full update can be found at Appendix A

- CPI rose to 2.3% in November 2018 before falling back to 1.9% in February 2019
- The unemployment was 3.9% in February 2019, the lowest rate since November 1974 to January 1975.
- The Bank of England increased the bank rate by 0.25% to 0.75% in August 2018.
- The data from the ONS Q4 Quarterly National Accounts published on 29 March 2019, showed that the UK economy expanded by 1.4% Year-on-Year

3.0 THE COUNCIL'S TREASURY POSITION.

3.1 The council's current strategy is to use internal borrowing to reduce risk and keep interest costs low. The treasury management change over the financial year is shown below.

	Balance at 01/04/2018 £m	Net Movement £m	Balance at 31/03/2019 £m
Long term borrowing - HRA	£73.9	-£1.1	£72.8
Long term borrowing – General Fund	£8.4	£0.0	£8.4
Other long-term liabilities - HBBC	£0.1	-£0.0	£0.1
Total Borrowing	**£82.4**	**-£1.1**	**£81.3**
Long term investments – greater than 1 year	£12.0	-£9.0	£3.0
Short term investments – less than 1 year	£29.3	£10.3	£39.6
Pooled funds and externally managed investments*	£2.6	£3.2	£5.8
Total Investments	**£43.9**	**£4.5**	**£48.4**
Net debt	**£38.5**	**-£5.6**	**£32.9**

*Represents investments held in Money Market Funds

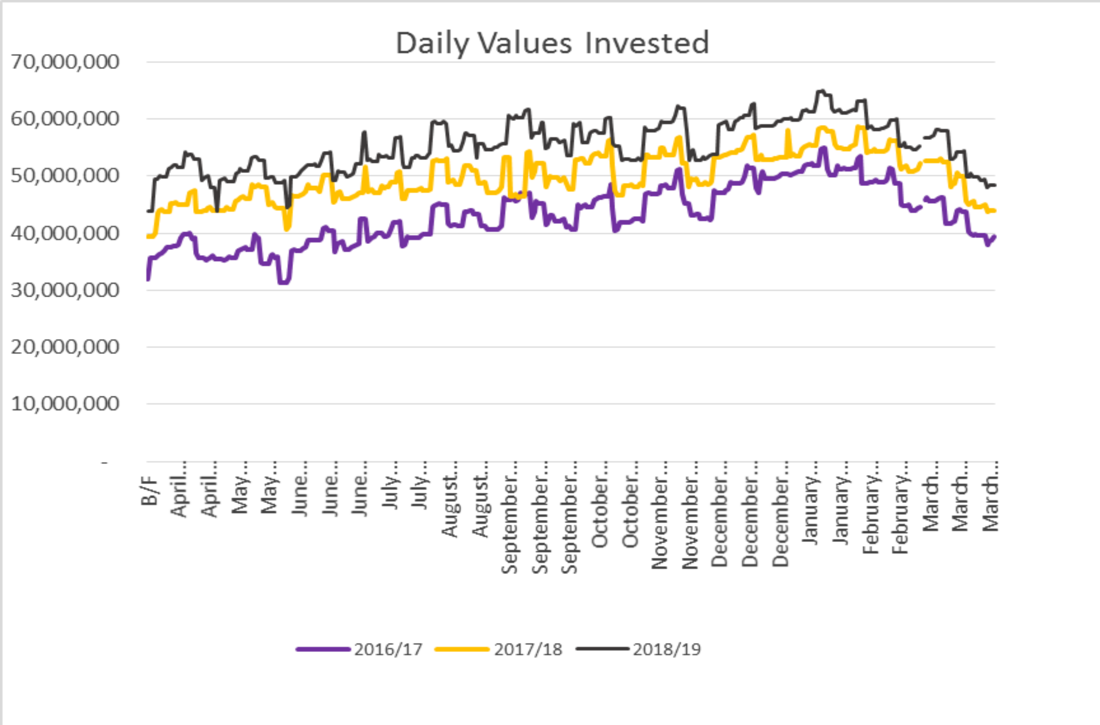
3.2 Annual repayments on two PWLB annuity loans (totalling £1.1m) taken out as part of the self-financing system of Council Housing in 2011/2012, is shown in the Net Movement column.

3.3 In 2018/19, the capacity for investment has increased by £4.5m. This can be affected by various factors including: increased income, contributions to/from reserves, setting aside expenditure to repay borrowing (MRP), fortuitous income, cash flow timing of receipts and payments and internal borrowing.

3.4 In 2018/19, some of the highlights that have increased investment capacity are:

- sales of assets – circa £3.3m including £3.2m HRA dwellings under Right to Buy, £65k in relation to one non-Right to Buy Housing asset and £25k for a disposal of a fleet vehicles through auction;
- MRP £0.55m, this is the amount charged to the revenue budget for repayment of debt. MRP is an accounting treatment, whereby we are providing an amount each year to repay debt created by capital expenditure;
- increased income from various activities across the council including:
    - circa £158k from investment income;
    - £130k from Development Control fees; and
    - £56k from recycling income.

3.5 The pattern of investments per day is shown in the table below, illustrating the cash flow trends throughout the year



4.0 BORROWING ACTIVITY.

4.1 The council's Borrowing Strategy 2018/19, incorporates a prudent and pragmatic approach to borrowing to minimise borrowing costs without compromising the longer-term stability of the portfolio, consistent with the council's Prudential Indicators.

4.2 No loans matured in 2018/19 that required replacement.

4.3 The Borrowing Strategy identified that borrowing would not be required until 2020/21 and the council has not undertaken any new long-term borrowing during the year. Interest payments totalling £2.74m were made in respect of existing debt.

4.4 The council's cash flow remained positive and did not require any temporary loans during the year.

4.5 The council had approximately £7.1m of internal debt at 31 March 2019. This is the cumulative value of internal cash balances used to finance new capital expenditure instead of financing through unsupported borrowing. This is currently judged to be the most cost effective means of funding the capital programme.

4.6 The estimated Minimum Revenue Provision (MRP) is intended to ensure that the capital financing debt is paid off over the longer term. The MRP charge made to General Fund revenue account for 2018/19 is £0.55m.

4.7 The Housing Revenue Account is not required to make MRP charges. However, the council classes the principal repayments made in respect of the two PWLB annuity loans taken out as part of the housing self-financing in 2011/12, as MRP. In 2018/19, this repayment was £1.1m.

5.0 DEBT RESCHEDULING ACTIVITY.

5.1 The council's Debt Rescheduling Strategy 2018/19, establishes a flexible approach where the rationale for rescheduling could be one or more of the following:

- Savings in interest costs with minimal risk.
- Balancing the volatility profile (i.e. the ratio of fixed to variable rate debt) of the debt portfolio.
- Amending the profile of maturing debt to reduce any inherent refinancing risks.

5.2 No opportunities for debt rescheduling were identified which conformed to the above rationale. Accordingly, the council has undertaken no debt rescheduling activity during the year.

5.3 The council's portfolio of thirteen loans - ten PWLB loans and three market loans continue to be monitored for debt rescheduling opportunities.

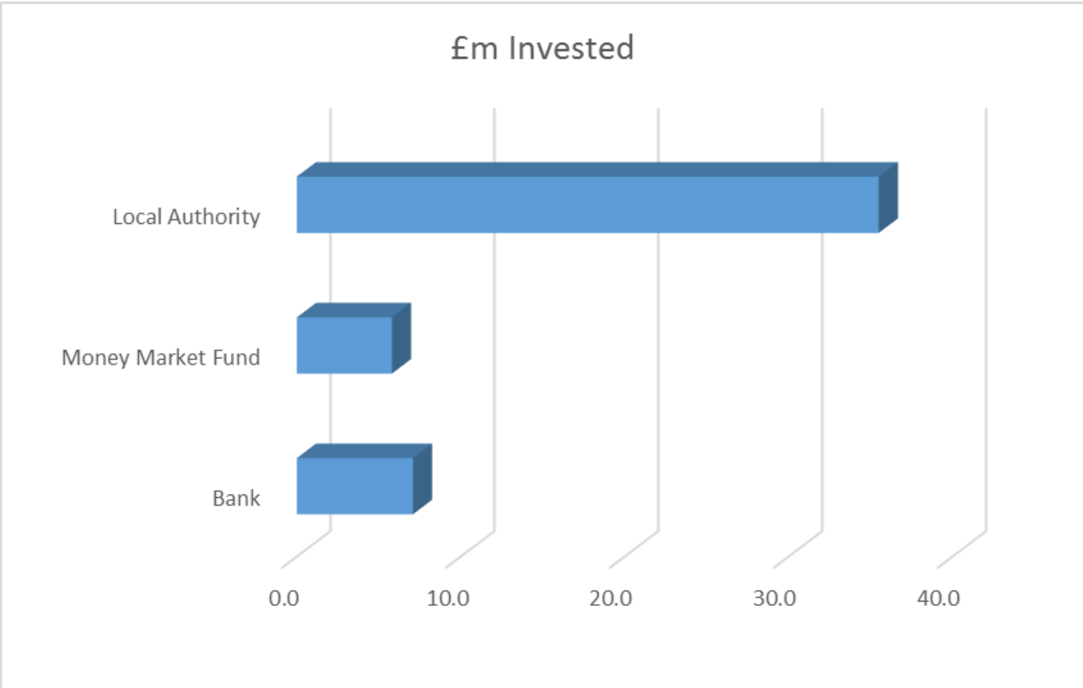
6.0 TREASURY MANAGEMENT INVESTMENT ACTIVITY.

6.1 The main objective of the council's Investment Policy and Strategy 2018/19 is to invest its surplus funds prudently.

6.2 The council's investment priorities (S.L.Y.) are:

- **S**ecurity of the invested capital;
- sufficient **L**iquidity to permit investments; and,
- Optimum **Y**ield which is commensurate with security and liquidity.

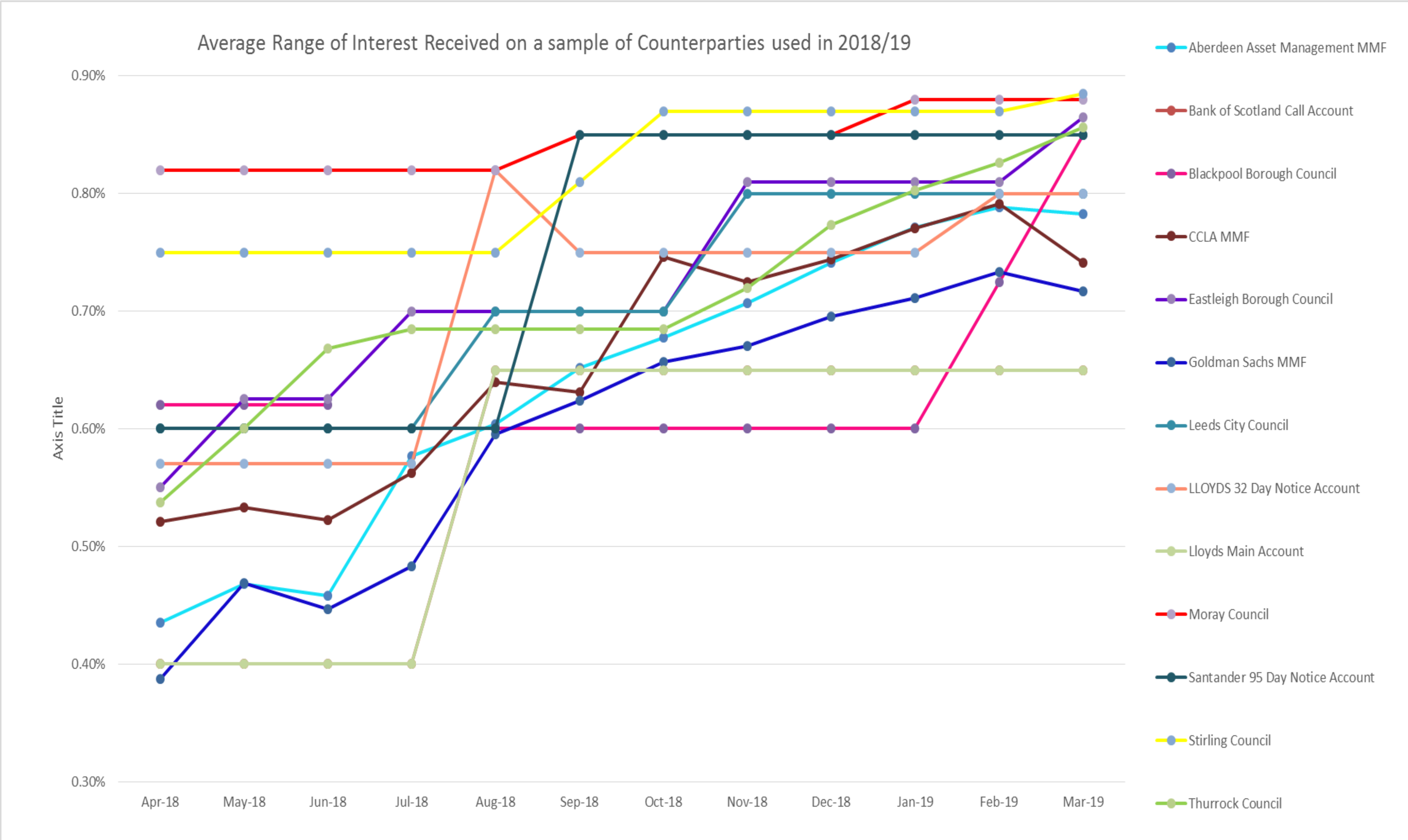
6.3 To lower the inherent investment risk, the council has minimised the use of banks and increased the use of other Local Authorities as investment counterparties. A range of lengths of investment, from overnight investments to short and long fixed term, from 32 days to 3 years, are currently utilised to ensure that the principles of security, liquidity and yield are followed. The table below shows the range of counterparties used by the council and the values invested at 31 March 2019.



6.4 The counterparties that the council currently use all meet the criteria set out in the Treasury Management Strategy Statement 2018/19 and are monitored by the Treasury Management Advisors. A detailed list of the counterparties used and amounts currently invested can be seen in Appendix B.

6.5 The average rate of return on the council's investment balances for the year was 0.71%. For comparison purposes, the benchmark return (average 7-day London Interbank Bid Rate or LIBID rate) on 29 March 2019 was 0.51% and the average 7 day London Interbank Offered Rate (LIBOR) rate was 0.63%. This shows that we are achieving a good rate of return against benchmark.

6.6 Paragraph 6.5 above explains that the current average rate of return of 0.71% has been achieved. The graph below shows the average rate over a sample of counterparties to illustrate the range and movement of interest rates over the year.

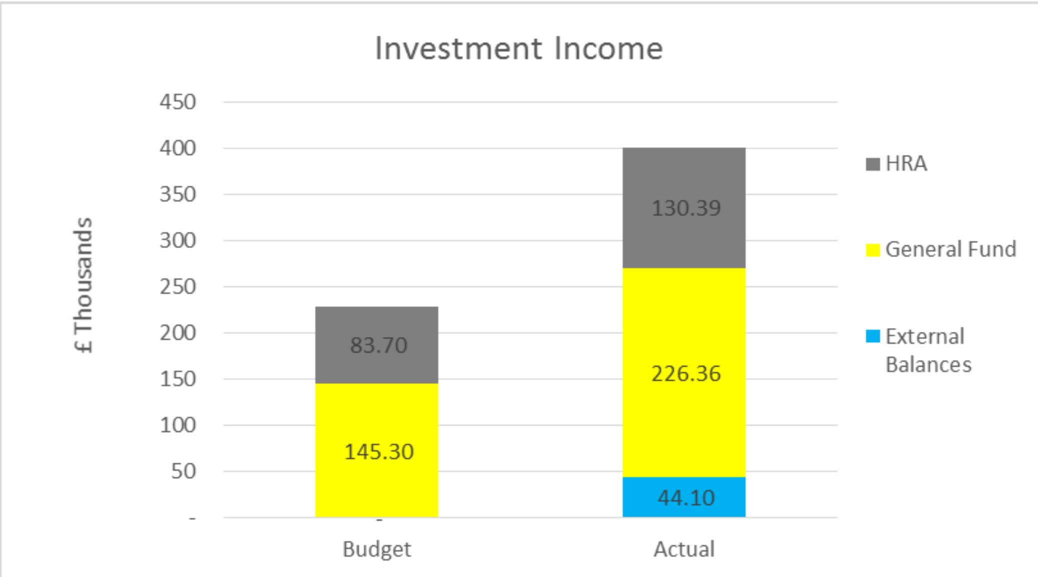

Average Range of Interest Received on a sample of Counterparties used in 2018/19
0.90%
0.80%
0.70%
0.60%
0.50%
0.40%
0.30%
Axis Title
Apr-18
May-18
Jun-18
Jul-18
Aug-18
Sep-18
Oct-18
Nov-18
Dec-18
Jan-19
Feb-19
Mar-19
Aberdeen Asset Management MMF
Bank of Scotland Call Account
Blackpool Borough Council
CCLA MMF
Eastleigh Borough Council
Goldman Sachs MMF
Leeds City Council
LLOYDS 32 Day Notice Account
Lloyds Main Account
Moray Council
Santander 95 Day Notice Account
Stirling Council
Thurrock Council

6.7 The council budgeted to achieve £229,000 of income from its investment activity in 2018/19 of which £145,300 is applied to General Fund and £83,700 to Housing Revenue Account. Investment activity for the year achieved £400,852 in interest.

6.8 Of the income achieved, an element is applied to balances held on external income. This external income largely represents balances from S106 contributions that have not yet been spent. The amount to be applied is £44,104. This is not budgeted for as S106 contributions are only achieved when specific conditions are met and are anticipated to be spent.

6.9 The remaining balance of £356,748 is apportioned between the General Fund, which will receive £226,356; and Housing Revenue Account which will receive £130,392.

6.10 The budgeted and projected levels of investment income is represented in the table below.



6.11 There were two breaches of investment limits in the year reported to Audit and Governance committee on 20 March 2019.

6.12 On 31 December 2018 the limit was breached by circa £143,000 due to income being processed earlier than it should have been. This was a banking day but the offices were closed. On 15 January 2019, the limit was breached by circa £90,000 due to a large S106 payment made to us by cheque which cleared overnight. These events were not something the council could have taken action to avoid.

7.0 NON-TREASURY INVESTMENT ACTIVITY

7.1 The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Authority as well as other non-financial assets which the Authority holds primarily for financial return. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return.

7.2 The following list represents the council's current investments in this area.

Property or Type	Value at 31 Mar 2018	Reason held
Industrial Units	£6.5m	To support the local economy and to generate profits to supplement council expenditure
Markets	£1.5m	Any profit supplements council expenditure
Land	£4.6m	Future economic benefit

7.3 More detailed information can be found in the "Investment Strategy – Service and Commercial" which was presented to Council on 26 February 2019.

7.4 From 2019/20, regular reports on non-treasury investment activity will be presented to Cabinet and/or Audit and Governance Committee.

8.0 SUMMARY

8.1 For the financial year 2018/19, the council can confirm that it has complied with its Prudential Indicators, which were approved as part of the council's Treasury Management Strategy Statement.

8.2 The council can confirm that during the financial year, other than the breach of prescribed limit detailed in paragraph 6.12, it has complied with its Treasury Management Practices.

APPENDIX A

Economic information provided by Treasury Management Advisors

External Context *(based on data as at 08/04/19)*

Economic commentary

Economic background: After spiking at over $85/barrel in October 2018, oil prices fell back sharply by the end of the year, declining to just over $50 in late December before steadily climbing toward $70 in April 2019. UK Consumer Price Inflation (CPI) for February 2019 was up 1.9% year/year, just above the consensus forecast but broadly in line with the Bank of England's February Inflation Report. The most recent labour market data for the three months to January 2019 showed the unemployment rate fell to a new low 3.9% while the employment rate of 76.1% was the highest on record. The 3-month average annual growth rate for pay excluding bonuses was 3.4% as wages continue to rise steadily and provide some upward pressure on general inflation. Once adjusted for inflation, real wages were up 1.4%.

After rising to 0.6% in the third calendar quarter from 0.4% in the second, fourth quarter economic growth slowed to 0.2% as weaker expansion in production, construction and services dragged on overall activity. Annual GDP growth at 1.4% continues to remain below trend. Following the Bank of England's decision to increase Bank Rate to 0.75% in August, no changes to monetary policy have been made since.

The US Federal Reserve continued its tightening bias throughout 2018, pushing rates to the 2.25%-2.50% range in December. However, a recent softening in US data caused the Fed to signal a pause in hiking interest rates at the last Federal Open Market Committee (FOMC) meeting in March.

With the 29th March 2019, the original EU 'exit day' now been and gone, having failed to pass a number of meaningful votes in Parliament, including voting down Theresa May's deal for the third time, MPs voted by a majority of one (313 to 312) to force the prime minister to ask for an extension to the Brexit process beyond 12th April in order to avoid a no-deal scenario. Recent talks between the Conservative and Labour parties to try to reach common ground on a deal which may pass a vote by MPs have yet to yield any positive results. The EU must grant any extension and its leaders have been clear that the terms of the deal are not up for further negotiation. The ongoing uncertainty continues to weigh on sterling and UK markets.

While the domestic focus has been on Brexit's potential impact on the UK economy, globally the first quarter of 2019 has been overshadowed by a gathering level of broader based economic uncertainty. The US continues to be set on a path of protectionist trade policies and tensions with China in particular, but with the potential for this to spill over into wider trade relationships, most notably with EU. The EU itself appeared to be show signs of a rapid slowdown in economic growth with the major engines of its economy, Germany and France, both suffering misfires from downturns in manufacturing alongside continued domestic/populist unrest in France. The International Monetary Fund downgraded its forecasts for global economic growth in 2019 and beyond as a consequence.

Financial markets: December was a month to forget in terms of performance of riskier asset classes, most notably equities. The FTSE 100 (a good indicator of global corporate sentiment) returned -8.8% assuming dividends were reinvested; in pure price terms it fell around 13%. However, since the beginning of 2019 markets have rallied, and the FTSE 100 and FTSE All share indices were both around 10% higher than at the end of 2018.

Gilt yields continued to display significant volatility over the period on the back of ongoing economic and political uncertainty in the UK and Europe. After rising in October, gilts regained their safe-haven status throughout December and into the New Year - the 5-year benchmark gilt yield fell as low as 0.80% and there were similar falls in the 10-year and 20-year gilts over the same period dropping from 1.73% to 1.08% and from 1.90% to 1.55%. The increase in Bank Rate pushed up money markets rates over the year and 1-month, 3-month and 12-month LIBID (London Interbank Bid) rates averaged 0.53%, 0.67% and 0.94% respectively over the period.

Recent activity in the bond markets and PWLB interest rates highlight that weaker economic growth is not just a UK phenomenon but a global risk. During March the US yield curve inverted (10-year Treasury yields were lower than US 3 month money market rates) and German 10-year Bund yields turned negative. The drivers are a significant shift in global economic growth prospects and subsequent official interest rate expectations given its impact on inflation expectations. Further to this is world trade growth which collapsed at the end of 2018 falling by 1.8% year-on-year. A large proportion of this downturn in trade can be ascribed to the ongoing trade tensions between the US and China which despite some moderation in January does suggest that the International Monetary Fund's (IMF) and Organisation for Economic Co-Operation & Development's (OECD) forecasts for global growth in 2019 of 3.5% might need to be revised downwards.

Credit background: Credit Default Swap (CDS) spreads drifted up towards the end of 2018 on the back of Brexit uncertainty before declining again in 2019 and continuing to remain low in historical terms. After hitting around 129 basis points in December 2018, the spread on non-ringfenced bank NatWest Markets plc fell back to around 96bps at the end of March, while for the ringfenced entity, National Westminster Bank plc, the CDS spread held relatively steady around 40bps. The other main UK banks, as yet not separated into ringfenced and non-ringfenced from a CDS perspective, traded between 33 and 79bps at the end of the period.

The ringfencing of the big four UK banks (Barclays, Bank of Scotland/Lloyds, HSBC and RBS/Natwest Bank plc) transferred their business lines into retail (ringfenced) and investment banking (non-ringfenced) entities.

In February, Fitch put the UK AA sovereign long-term rating on Rating Watch Negative as a result of Brexit uncertainty, following this move with the same treatment for UK banks and a number of government-related entities.

There were minimal other credit rating changes during the period. Moody's revised the outlook on Santander UK to positive from stable to reflect the bank's expected issuance plans which will provide additional protection for the its senior unsecured debt and deposits.

Appendix B

Counterparty	Length	From	To	Amount	Rate
Bank of Scotland	Overnight	31/03/19	01/04/19	1,295,000.00	0.65%
Barclays Treasury Direct Facility	92	07/03/19	07/06/19	1,500,000.00	0.68%
Blackpool Borough Council	181	06/02/19	06/08/19	2,000,000.00	0.85%
Broxtowe Borough Council	181	01/02/19	01/08/19	1,000,000.00	0.92%
CCLA MMF	Overnight	31/03/19	01/04/19	1,000,000.00	0.74%
Close Brothers Ltd	185	29/03/19	30/09/19	1,000,000.00	1.10%
Conwy County Borough Council	181	28/02/19	28/08/19	2,000,000.00	0.90%
Eastleigh Borough Council	165	15/11/18	29/04/19	1,000,000.00	0.83%
Eastleigh Borough Council	315	07/11/18	18/09/19	2,000,000.00	0.90%
Federated Investors MMF	Overnight	31/03/19	01/04/19	3,000,000.00	0.79%
Goldman Sachs MMF	Overnight	31/03/19	01/04/19	1,800,000.00	0.72%
Highland Council	269	26/02/19	22/11/19	2,000,000.00	1.05%
Kingston-upon-Hull City Council	183	26/11/18	28/05/19	1,500,000.00	0.90%
Kingston-upon-Hull City Council	112	19/12/18	10/04/19	2,500,000.00	0.90%
Leeds City Council	247	22/08/18	26/04/19	2,000,000.00	0.80%
Liverpool City Council	182	11/02/19	12/08/19	2,000,000.00	0.90%
Lloyds Bank Fixed Term Deposit	182	19/11/18	20/05/19	1,500,000.00	0.90%
Lloyds Main	Overnight	31/03/19	01/04/19	42,474.91	0.65%
Lloyds Notice Account	32 days	31/03/19	02/05/19	250,000.00	0.80%
Northumberland County Council	1096	03/04/17	03/04/20	3,000,000.00	0.99%
Santander Notice Account	95 days	31/03/19	04/07/19	1,495,000.00	0.85%
Slough Borough Council	183	28/02/19	30/08/19	2,500,000.00	0.98%
Slough Borough Council	306	29/03/19	29/01/20	2,000,000.00	1.00%
Stirling Council	254	17/09/18	29/05/19	1,500,000.00	0.87%
Stirling Council	91	29/03/19	28/06/19	1,000,000.00	0.90%
Surrey Heath Borough Council	181	15/11/18	15/05/19	1,000,000.00	0.95%
Thurrock Council	288	18/06/18	02/04/19	1,000,000.00	0.66%
Thurrock Council	191	19/11/18	29/05/19	1,000,000.00	0.86%
Thurrock Council	181	15/01/19	15/07/19	1,000,000.00	0.89%
Thurrock Council	181	08/02/19	08/08/19	1,000,000.00	0.92%
Thurrock Council	184	20/03/19	20/09/19	1,000,000.00	0.95%
Uttlesford District Council	185	21/01/19	25/07/19	1,500,000.00	0.92%
Total				**48,382,474.91**	