Council	Agenda Item:
Meeting Date	9 October 2019
Report Title	Annual Treasury Management Report 2018/19
Cabinet Member	Cllr Roger Truelove, Leader and Cabinet Member for Finance
SMT Lead	Nick Vickers, Chief Financial Officer
Head of Service	Nick Vickers, Chief Financial Officer
Lead Officer	Phil Wilson, Financial Services Manager/ Olga Cole, Management Accountant
Key Decision	No
Classification	Open

Recommendations	1. Approve the Treasury Management stewardship report for 2018/19.
	2. Approve the Prudential and Treasury Management Indicators within the report.

1. Purpose of Report and Executive Summary

1.1 The Council's Treasury Management activity is underpinned by the Chartered Institute of Public Finance and Accountancy's (CIPFA's) Code of Practice on Treasury Management ("the Code"), which requires local authorities to produce annual Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity. The Code also recommends that members are informed of Treasury Management activities at least twice a year.

1.2 Treasury Management is defined as "the management of the Council's 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". No Treasury Management activity is without risk; the effective identification and management of risk are integral to the Council's Treasury Management objectives.

1.3 For 2018/19 the Investments Section of the Kent County Council (KCC) Finance Department had operational responsibility for the daily treasury management duties in order to cover a maternity leave. KCC Finance in undertaking this work had to comply with this Council's Treasury Management Strategy. Overall responsibility for Treasury Management remained with the Council.

1.4 This report:

- is prepared in accordance with the CIPFA Treasury Management Code and the Prudential Code;

- details the implications of treasury decisions and transactions;
- gives details of the outturn position on Treasury Management transactions in 2018/19; and
- confirms compliance with Treasury limits and Prudential Indicators.

1.5 This report was submitted to the Audit Committee on 18 September 2019.

2. Background

Borrowing Requirement and Debt Management

2.1 The overall borrowing position is summarised below:

	Balance on 31/3/2018	Movement in Year	Balance on 31/3/2019
	£'000	**£'000**	**£'000**
Capital Financing Requirement	12,511	+15,254	27,765
Other Long-Term Liabilities (cost of leases for equipment)	(140)	+140	0
Borrowing Capital Financing Requirement	**12,371**	**15,394**	**27,765**
External Borrowing	0	(10,000)	(10,000)
Cumulative External Borrowing Requirement	**12,371**	**5,394**	**17,765**

2.2 Where capital expenditure is to be financed in future years by charges to revenue as assets are used by the Council, the expenditure results in an increase in the Capital Financing Requirement (CFR), a measure of the capital expenditure incurred historically by the Council that has yet to be financed.

2.3 The reason for the increase in the CFR in 2018/19 is due to the capital expenditure on works undertaken as part of the Sittingbourne Town Centre regeneration project and which were financed from borrowing. The CFR will be reduced in the future by contributions from rental income.

2.4 In 2018/19, the Council took out two loans of £5 million each, from other local authorities. One loan was for 12 months at a rate of 1.1% and the second loan was for 18 months at a rate of 1.2%.

Investment Activity

2.5 The Council holds significant investment funds, representing income received in advance of expenditure plus balances and reserves held. During 2018/19, the Council held average daily cash balances of £28 million, which is a decrease of £8 million on the previous year due to the level of expenditure on Sittingbourne Town Centre.

2.6 The Council's budgeted investment income for 2018/19 was £110,000 and the actual income received was £290,000, of which £132,000 was from the Council's long-term investment in the Church, Charities and Local Authorities (CCLA) Mutual Investment Property Fund. The CCLA investment has been a highly successful one for the Council as UK commercial property has continued to perform well. There was also an improvement in the rates paid on the Council's deposits as a result of the base rate rise in 2018/19.

2.7 The table below summarises the Council's investment portfolio at 31 March 2019. All investments made were in line with the Council's approved credit rating criteria at the time of placing the investment, and still met those criteria at 31 March 2019.

Counterparty **(MMF = Money Market Funds)**	**Long-Term Rating**	**Balance Invested at 31 March 2019** **£'000**
Invesco MMF	AAAmmf	3,000
Goldman Sachs MMF	AAAmmf	2,990
Morgan Stanley MMF	AAAmmf	3,000
Black Rock MMF	AAAmmf	3,000
Aberdeen MMF	AAAmmf	3,000
Amundi MMF	AAAmmf	3,000
Sub Total Cash & Cash Equivalents		**17,990**
CCLA Property Fund	unrated	3,000
Sub Total Long-Term Investments		**3,000**
Total		**20,990**

2.8 The ratings above are from Fitch credit rating agency. A description of the grading is provided below:

- AAAmmf: Funds have very strong ability to meet the dual objectives of providing liquidity and preserving capital.

2.9 The treasury management position for the year is summarised below:

Investments	**Balance on 31/03/18**	**Movement in Year**	**Balance on 31/03/19**	**Average Rate**
	£'000	**£'000**	**£'000**	**%**
Short-Term Investments and Cash and Cash Equivalents	16,815	1,175	17,990	0.90
Long-Term Investments	3,000	0	3,000	4.40
TOTAL INVESTMENTS	**19,815**	**1,175**	**20,990**	
Borrowing				
Long-Term Borrowing	0	(5,000)	(5,000)	1.21
Short-Term Borrowing	0	(5,000)	(5,000)	1.10
TOTAL BORROWING	**0**	**(10,000)**	**(10,000)**	

The long-term investment shown in the table above is the Council's investment in the CCLA Property Fund.

2.10 The Council's investment strategy has two overriding principles:

- Minimising the cost to the revenue budget - given the continued reductions in local government financing there is no scope within the revenue budget to meet debt charge costs. If the Council incurred debt charge costs then, unless the investment generated sufficient income to cover these costs, the Council may have to reduce services to fund the costs. In the case of the Sittingbourne Town Centre investment all the capital financing costs will be funded from rental income; and,

- Strategic impact - if the Council is going to invest in property it needs to support the Council's wider objectives around regeneration of the Council and creating new employment. This means there needs to be additionality in terms of the wider economic benefits e.g. higher business rates.

2.11 In keeping with the Ministry of Housing, Communities and Local Government's (MHCLG's) Guidance on Investments, the Council maintained a sufficient level of liquidity through the use of Money Market Funds, overnight deposits and the use of call accounts.

2.12 The Council sought to optimise returns commensurate with its objectives of security and liquidity.

2.13 The criteria applied by the Chief Financial Officer for the approval of a counter party for deposits are:

- credit rating - a minimum long-term of A-;
- credit default swaps;
- share price;
- reputational issues;
- exposure to other parts of the same banking group; and
- country exposure.

2.14 The investments permissible by the 2018/19 Treasury Strategy were:

Investment	Limit	Used in 2018/19?
Debt Management Office (Debt Management Account Deposit Facility) and Treasury Bills	Unlimited	Yes
Major UK banks / building societies. (Barclays, HSBC, Lloyds Banking Group, RBS Group, Santander UK, Nationwide, Standard Chartered) unsecured deposits	£3m	HSBC, Lloyds Bank
Svenska Handelsbanken unsecured deposits	£3m	No
Leeds Building Society unsecured deposits	£1.5m	No
Close Brothers unsecured deposits	£1.5m	No
Major overseas banks unsecured deposits (to be determined based upon Arlingclose advice) Netherlands: Bank Nederlande Gemeeten, Rabobank Singapore: OCBC, UOB, DBS Sweden: Nordea Bank Denmark: Danske Bank USA: JP Morgan Chase Australia: Australian and New Zealand Banking Group, Commonwealth Bank of Australia, National Australian Bank Ltd, Westpac Banking Corp Canada: Bank of Montreal, Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Royal Bank of Canada, Toronto Dominion Bank	£1.5m limit per bank, £3m country limit	No
Money Market Funds	£3m each	Yes
Cash Plus Funds and Short Dated Bond Funds	£3m each	No

Investment	Limit	Used in 2018/19?
Multi Asset Income Funds	£3m each	No
CCLA Property Fund	£3m	Yes
Supranational Bonds	£3m in aggregate	No
Corporate Bond Funds and Corporate Bonds	£3m in aggregate	No
Non-Treasury Investments	To be agreed on a case by case basis	Yes
Covered Bonds	£9m in aggregate with £3m limit per bank	No
Absolute Return Funds	£3m in aggregate	No
Equity Income Funds	£3m in aggregate	No

2.15 The maximum permitted duration for deposits is 13 months. The Chief Financial Officer in consultation with the Leader and Cabinet Member for Finance may consider longer duration. Bonds can be purchased with a maximum duration of five years.

2.16 The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. This is replicated in the MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return. In 2018/19, the Council held £3 million of such longstanding investments in 14 directly owned properties. These investments generated £0.2 million of investment income for the Council after taking account of direct costs, representing a rate of return of 5%.

External Context

2.17 The Bank of England's Monetary Policy Committee (MPC) increased the Bank Rate by 0.25% in August 2018 to 0.75%, no changes to monetary policy have been made since.

2.18 The Council has seen a dramatic change over the last nine years in how it is funded. The Revenue Support Grant will disappear completely in 2020/21, and in its place the Council has become reliant on income sources that are related in full or in some part to issues over which it has control. This sets the pattern for how councils will be funded in the future.

Compliance

2.19 The Council has complied with its Prudential and Treasury Management Indicators for 2018/19 which were set as part of the Treasury Management Strategy agreed by Council in February 2018.

2.20 In Appendix I the outturn position for the year against each Prudential Indicator is set out.

2.21 The Chief Financial Officer confirms that all treasury management activities undertaken during the year complied fully with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy

Treasury Advisers

2.22 Arlingclose has been the Council's treasury advisers since May 2009. The current contract had an option of a two-year extension and this was taken up in May 2019. Officers of the Council meet with Arlingclose regularly and high quality and timely information is received from them.

Capital Strategy

2.23 The 2017 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy, complying with CIPFA's requirement, was approved by Council on 20 February 2019.

3. Proposal

3.1 Members are asked to approve the report.

4. Alternative Proposals

4.1 The alternative is not to comply with the mandatory CIPFA Code. This is not something which the S151 Officer can recommend.

5. Consultation Undertaken

5.1 Arlingclose have been consulted.

6. Implications

Issue	**Implications**
Corporate Plan	Supports delivery of the Council's objectives.
Financial, Resource and Property	As detailed in the report

Issue	Implications
Legal, Statutory and Procurement	CIPFA produce a framework for managing treasury activities, called a ‘Code’. Councils are legally required to have regard to this Code and members of CIPFA are expected to comply with its requirements. 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 Guidance
Crime and Disorder	Not relevant to this report
Environment and Sustainability	Not relevant to this report
Health and Wellbeing	Not relevant to this report
Risk Management and Health and Safety	Not relevant to this report
Equality and Diversity	Not relevant to this report
Privacy and Data Protection	Not relevant to this report

7. Appendices

7.1 Appendix I: Treasury Management and Prudential Indicators

8. Background Papers

None

Treasury Management and Prudential Indicators for 2018/19

Introduction

The Local Government Act 2003 requires the Council to have regard to the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

This report compares the approved indicators with the outturn position for 2018/19. Actual figures have been taken from or prepared on a basis consistent with, the Council's Statement of Accounts

Capital Expenditure: The Council's capital expenditure and financing may be summarised as follows.

Capital Expenditure and Financing	**2018/19 Estimate**	**2018/19 Actual**	**2018/19 Difference**
	£'000	**£'000**	**£'000**
Total Capital Expenditure	**20,347**	**18,871**	**(1,476)**
Capital Receipts	107	438	331
Grants and Other Contributions	3,666	2,382	(1,284)
Reserves	434	359	(75)
Internal/External Borrowing	16,140	15,692	(448)
Total Financing	**20,347**	**18,871**	**(1,476)**

Treasury Management and Prudential Indicators for 2018/19

Capital Financing Requirement: The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose.

Capital Financing Requirement	31/03/19 Estimate	31/03/19 Actual	31/03/19 Difference
	£'000	£'000	£'000
Total CFR	41,572	27,765	(13,807)
Less: Other Long-Term Liabilities	(41)	0	41
Borrowing CFR	**41,531**	**27,765**	**(13,766)**
External Borrowing	(26,522)	(10,000)	16,522
Cumulative External Borrowing Requirement	**15,009**	**17,765**	**2,756**

External borrowing: as at 31 March 2019 the Council had £10 million of external borrowing.

Operational Boundary for External Debt: The Operational Boundary is based on the Council's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Council's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance lease, and other liabilities that are not borrowing but form part of the Council's debt.

Operational Boundary and Total Debt	31/03/19 Boundary	31/03/19 Actual Debt	Complied
	£'000	£'000	
Borrowing	55,000	10,000	✓
Other Long-Term Liabilities	24	0	✓
Total Operational Boundary	**55,024**	**10,000**	✓

Treasury Management and Prudential Indicators for 2018/19

Authorised Limit for External Debt: The Authorised Limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Council can legally owe. The Authorised Limit provides headroom over and above the Operational Boundary for unusual cash movements.

Authorised Limit and Total Debt	31/03/19 Boundary	31/03/19 Actual Debt	Complied
	£'000	£'000	
Borrowing	60,000	10,000	✓
Other Long-Term Liabilities	2,000	0	✓
Total Authorised Limit	**62,000**	10,000	✓

The Chief Financial Officer confirms that there were no breaches to the Authorised Limit and the Operational Boundary during 2018/19.

Ratio of Financing Costs to Net Revenue Stream: This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

Ratio of Financing Costs to Net Revenue Stream	31/03/19 Estimate	31/03/19 Actual	Difference
	%	%	%
General Fund Total	7.01	0.94	6.07

Interest Rate Exposures: This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of net interest payable was:

Interest Rate Exposures	31/03/19 Actual	2018/19 Limit	Complied
	%	%	
Interest on Fixed Rate Investments	0	-100	✓
Interest on Variable Rate Investments	-100	-100	✓
Interest on Fixed Rate Borrowing	100	100	✓
Interest on Variable Rate Borrowing	0	100	✓

Treasury Management and Prudential Indicators for 2018/19

Maturity Structure of Borrowing: This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing were:

	31/03/19 Actual	Upper Limit	Lower Limit	Complied
	%	%	%	
Under 12 months	50	100	0	✓
12 months and within 24 months	50	100	0	✓
24 months and within 5 years	0	100	0	✓
5 years and within 10 years	0	100	0	✓
10 years and above	0	100	0	✓

Principal Sums Invested for Periods Longer than 364 days: The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end were:

	2018/19
	£'000
Actual Principal Invested Beyond Year End	3,000
Limit on Principal Invested Beyond Year End	10,000
Complied	✓

Investment Benchmarking

Average Actual Return on Investments 2018/19	Original Estimate Return on Investments 2018/19	Average Bank Rate 2018/19	Average 7-day LIBID Rate 2018/19
0.90%	0.39%	0.67%	0.51%

(The London Interbank Bid Rate (LIBID) is a bid rate; the rate at which a bank is willing to borrow from other banks)