

## **COUNCIL**

### **REPORT OF THE DIRECTOR OF FINANCE AND CORPORATE SERVICES – MR HYWEL JENKINS**

**26<sup>th</sup> SEPTEMBER 2018**

#### **SECTION A – MATTERS FOR INFORMATION**

**WARDS AFFECTED: ALL**

#### **ANNUAL TREASURY MANAGEMENT OUTTURN REPORT 2017/18**

##### **1. Purpose of Report**

- 1.1 This Council is required through regulations issued under the Local Government Act 2003 to produce an annual treasury report reviewing treasury management activities and the actual prudential and treasury indicators for 2017/18 (this report).
- 1.2 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). Some information incorporated within this report has been provided by the Council's Treasury Advisors Link Asset Services.
- 1.3 Recent changes in the regulatory environment place a much greater onus on members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.
- 1.4 This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to the annual strategy report, which was submitted to Cabinet in February 2017 before being reported to full Council.

## 2.0 Executive Summary

2.1 During 2017/18, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

<b>Prudential and Treasury Indicators</b>	<b>2016/17 Actual £000</b>	<b>2017/18 Mid-Year Estimate £000</b>	<b>2017/18 Actual £000</b>
Capital Expenditure	53,758	76,366	68,963
Capital Financing Requirement	292,824	321,819	325,241
External debt(gross)	250,140	255,654	265,655
Less Investments	(70,820)	(60,000)	(61,000)
<b>Net Borrowing</b>	<b>179,320</b>	<b>195,654</b>	<b>204,655</b>

2.2 The full list of prudential and treasury indicators are to be found in Appendix 1. During the financial year the Council operated within its treasury limits and Prudential Indicators.

The financial year 2017/18 was once again a challenging environment as in previous years with low investment returns and continuing counterparty risk.

## 3.0 Introduction and Background

3.1 This report summarises:

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- Reporting of the required prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and

- Detailed investment activity

#### 4.0 The Council's Capital Expenditure and Financing 2017/18

4.1 The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

4.2 Actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

	<b>2016/17 Actual £'000</b>	<b>2017/18 Mid-Year Estimate £'000</b>	<b>2017/18 Actual £'000</b>
Total capital expenditure	53,758	76,366	68,963
Resourced by:			
• Capital receipts *	1,412	1,300	0
• Capital grants & contributions	19,870	37,827	30,345
• Direct Revenue Financing	2,441	67	605
<b>Unfinanced capital expenditure (to be funded from Borrowing)</b>	<b>30,035</b>	<b>37,172</b>	<b>38,013</b>

\* Capital receipts are currently being retained to fund potential future City Deal revenue expenditure.

#### 5.0 The Council's Overall Borrowing Need

5.1 The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a

gauge of the Council's debt position. The CFR results from the capital activity of the Council and what resources have been used to pay for the capital spend. It represents the 2017/18 unfinanced capital expenditure (see Table 2) and prior years' net of unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

- 5.2 Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board [PWLB] or the money markets), or utilising temporary cash resources within the Council.
- 5.3 Reducing the CFR – Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision – MRP, to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.
- 5.4 The total CFR can also be reduced by:
- The application of additional capital financing resources (such as unapplied capital receipts); or
  - Charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).
- 5.5 The Council's CFR for the year is shown below, and represents a key prudential indicator.

<b>CFR</b>	<b>2016/17 Actual £'000</b>	<b>2017/18 Mid-Year Estimate £'000</b>	<b>2017/18 Actual £'000</b>
Opening balance	270,244	292,826	292,824
Add unfinanced capital expenditure (as above)	30,035	37,172	38,013
Less MRP	(7,455)	(8,179)	(8,433)
Adjustment re: finance lease #			2,837
<b>Closing balance</b>	<b>292,824</b>	<b>321,819</b>	<b>325,241</b>

# Adjustment required as a result of the requirement to account for future finance lease payments in respect of the Gwalia residential care contract.

- 5.6 The borrowing activity is constrained by prudential indicators for net borrowing and the CFR, and by the authorised limit.
- 5.7 Net borrowing and the CFR – in order to ensure that borrowing levels are prudent over the medium term the Council's external borrowing, net of investments, must only be used for a capital purpose. This essentially means that the Council is not borrowing to support revenue expenditure. Net borrowing should not therefore, except in the short term, have exceeded the CFR for 2017/18 plus the expected changes to the CFR over 2018/19 and 2019/20. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2017/18. The table below highlights the Council's net borrowing position against the CFR. The Council has complied with this prudential indicator.

	<b>31/3/17 Actual £'000</b>	<b>31/3/18 Mid-Year Estimate £'000</b>	<b>31/3/18 Actual £'000</b>
Net borrowing position	179,320	195,654	204,655
CFR	292,824	321,819	325,241

- 5.8 The authorised limit – the authorised limit is the “affordable borrowing limit” required by s3 of the Local Government Act 2003. The Council does not have the power to borrow above this level.
- 5.9 The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

	<b>Actual 2017/18 £000</b>
Operational boundary	327,607
Authorised limit	347,607
Total Maximum Borrowing compared to Operational Boundary at any point during the year	267,696

The Council has maintained gross borrowing below the Authorised limit.

## 6.0 Treasury Position as at 31<sup>st</sup> March 2018

- 6.1 The Council’s debt and investment position is managed by Finance Treasury Staff in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through Member reporting detailed in the executive summary, and through officer activity detailed in the Council’s Treasury Management Practices. At the beginning and the end of 2017/18 the Council’s treasury position was as follows:

	<b>31 March 2017 Principal</b>	<b>Rate / Return</b>	<b>31 March 2018 Principal</b>	<b>Rate / Return</b>
Fixed rate funding:	<b>£m</b>	<b>%</b>	<b>£m</b>	<b>%</b>
-PWLB	174.712	4.34	203.155	3.96
-Market (Rifw & LOBO)	75.428	3.69	62.500	3.92
<b>Total debt</b>	<b>250.140</b>	<b>4.00</b>	<b>265.655</b>	<b>3.83%</b>

Investments:				
- in house	70.820	0.70	61.000	0.67%
<b>Total investments</b>	<b>70.820</b>	<b>0.70</b>	<b>61.000</b>	<b>0.67%</b>

PWLB = Public Works Loans Board which is a body the Government has established to lend money to Local Government.

Market LOBO's = Lender Option Borrower Option – this is borrowing from the market when the lender has offered a long term loan but with options to continue or foreclose on the loan at various specific intervals.

## 7.0 The Strategy for 2017/18

7.1 The strategy for 2017/18 was approved by Council in February 2017 and included the following:

### 7.2 New Borrowing:

The cheapest borrowing will be internal borrowing by running down cash balances and foregoing interest earned at historically low rates. However this strategy can only be used as a short term measure therefore consideration will be given to entering into external borrowing.

The following types of loan arrangement will be considered (in no particular order):

- Temporary borrowing from the money markets or other local authorities.
- Short dated borrowing from the market or PWLB.
- Long term fixed rate market or PWLB loans

### 7.3 Investments

The Council continued with its main investment priorities:

- (a) security of capital
- (b) liquidity of capital

with the aim of achieving the optimum return commensurate with proper levels of security and liquidity. With investments being

dominated by low counterparty risk considerations, relatively low returns were expected when compared to borrowing rates.

7.4 For balances generated through normal cashflow the strategy looked to utilise the business reserve (call account) and short dated deposits.

7.5 Debt Rescheduling

The strategy did allow for the use of investment balances to repay debt prematurely providing it was economically worthwhile and it enhanced the maturity profile of the debt portfolio.

No debt rescheduling was anticipated (or took place) in 2017/18 particularly as the PWLB rate structures have made it more expensive in recent years to do so.

8. **Borrowing Outturn for 2017/18**

8.1 The following long term loans were entered into during 2017/18 due to the fact that PWLB loan rates were at historic low rates. These loans are used to finance capital expenditure on projects such as the 21<sup>st</sup> Century Schools Programme, Street Lighting Replacement Programme and Regeneration.

<b>Lender</b>	<b>Date</b>	<b>Amount £'000</b>	<b>Rate %</b>	<b>Period</b>	<b>Details</b>
PWLB	15/8/17	10,000	2.33	48.5yrs	Maturity
PWLB	23/11/17	10,000	2.43	41.5yrs	Maturity
PWLB	23/11/17	10,000	2.42	42.5yrs	Maturity

8.2 Treasury Borrowing – The following short term temporary loans were undertaken during the year:-

<b>Start Date</b>	<b>End Date</b>	<b>Lender</b>	<b>Value £'000</b>	<b>Rate %</b>
27/9/17	6/10/17	Leeds City Council	5,000	0.20
27/10/17	2/11/17	Middlesborough Borough Council	2,000	0.18
3/11/17	10/11/17	Northern Ireland Housing Executive	3,000	0.26





8.3 Rescheduling – No loans were rescheduled during 2017/18

9. **Investment Outturn for 2017/18**

9.1 Investment Policy – the Council’s investment policy is governed by Welsh Government guidance, which has been implemented in the annual investment strategy approved by Council in February 2017. 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 (such as rating outlooks, credit default swaps, bank share prices etc).

9.2 The investment activity during the year conformed to the approved strategy.

9.3 Resources – the Council’s longer term cash balances comprise, primarily, revenue and capital resources, although these will be influenced by cash flow considerations. The Council’s core cash resources comprised the following:

<b>Balance Sheet Resources</b>	<b>31 March 2017 £'000</b>	<b>31 March 2018 £'000</b>
Balances and Earmarked Reserves	51,277	59,469
Provisions	7,154	6,345
Usable capital receipts	5,641	6,800
<b>Total</b>	<b>64,072</b>	<b>72,614</b>

9.4 Investments held by the Council – The Council received the following return on its investments:

<b>Average Investment £'000</b>	<b>External Interest Earned £'000</b>	<b>Rate of Return %</b>	<b>Benchmark Return %</b>
79,112	527	0.67	0.39

The benchmark for funds managed in house is the 3 month LIBID uncompounded. The rate reflects a more realistic neutral position

for core investments with a medium term horizon and a rate which is more stable with fewer fluctuations caused by market liquidity.

## **10. Performance Measurement**

- 10.1 One of the key requirements in the Code is the formal introduction of performance measurement relating to investments, debt and capital financing activities. Whilst investment performance criteria have been well developed and universally accepted, debt performance indicators continue to be a more problematic area with the traditional average portfolio rate of interest acting as the main guide (as incorporated in the table in section 6). The Council's original performance indicators for 2017/18 were set out in the Annual Treasury Strategy approved by Council in February 2017.

## **11. Financial Impact**

All financial impacts are detailed within the body of the report.

## **12. Integrated Impact Assessment**

There is no requirement for an integrated impact assessment for this report.

## **13. Workforce impacts**

There are no workforce impacts resulting from this report.

## **14. Legal impacts**

The report deals with the Council's legal requirements as set out in Local Government Act 2003.

## **15. Risk management**

Compliance with the strategies outlined in this report should be sufficient in terms of managing risks in this area.

## **16. Recommendations**

It is recommended that Members note the 2017/18 treasury management function performance as set out in this report including the actual 2017/18 prudential and treasury indicators.

## 17. **Appendices**

### Appendix 1 – Prudential Indicators

#### **List of Background Papers**

Treasury Management Closing Files 2017/18

Link Asset Services - Treasury Management Templates

#### **Officer Contact**

For further information on this report item, please contact: -

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<b>PRUDENTIAL INDICATORS</b>	<b>2016/17 Actual</b>	<b>2017/18 Mid-Year Estimate</b>	<b>2017/18 Actual</b>
Capital Expenditure	<b>£'000</b> 53,758	<b>£'000</b> 76,366	<b>£'000</b> 68,963
Capital Financing Requirement as at 31 <sup>st</sup> March	292,824	321,819	325,241
Ratio of financing costs to net revenue stream	<b>%</b> 6.20	<b>%</b> 6.36	<b>%</b> 6.84
<b>Authorised Limit for External Debt:</b> Borrowing and other long term liabilities	343,791	347,607	347,607
<b>Operational Boundary for External Debt:</b> Borrowing and other long term liabilities	323,791	327,607	327,607
<b>External Debt (Gross)</b>	250,140	255,654	265,655
Less Investments	(70,820)	(60,000)	(61,000)
<b>Net Borrowing Position</b>	<b>179,320</b>	<b>195,654</b>	<b>204,655</b>

<b>Maturity Structure of Fixed Rate Borrowing During 2017/18</b>	<b>2016/17 Actual</b>	<b>2017/18 Original Estimate</b>		<b>2017/18 Actual</b>
		<b>Upper Limit</b>	<b>Lower Limit</b>	
	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>
Under 12 months	6	15	0	3
12 months to 2 years	2	15	0	2
2 to 5 years	7	40	0	6
5 to 10 years	7	60	0	5
10 years and above	78	100	15	84