Cyngor Castell-nedd Port Talbot
Neath Port Talbot Council

NEATH PORT TALBOT COUNTY BOROUGH COUNCIL

CABINET

REPORT OF THE DIRECTOR OF FINANCE & CORPORATE SERVICES

20th NOVEMBER 2019

MATTERS FOR INFORMATION

WARDS AFFECTED - ALL

TREASURY MANAGEMENT MID YEAR REVIEW REPORT 2019/20

Purpose of the Report

1. To review treasury management activities for the 6 month period to 30th September 2019.

Background

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

3. The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

4. As a consequence treasury management is defined as:

"The management of the local authority'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. "

Introduction

5. The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2011) was adopted by this Council at the Council meeting in 28th February 2013.

The primary requirements of the Code are as follows:

(i) Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

(ii) Creation and maintenance of Treasury Management Practices set out in the manner in which the Council will seek to achieve those policies and objectives.

(iii) Receipt by the full 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 (stewardship report) covering activities during the previous year.

(iv) 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.

(v) Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated bodies are the Audit and Policy and Resources Committees.

Scheme of Delegation

Area of Responsibility	**Council/ Committee**	**Frequency**
Treasury Management Strategy / Annual Investment Strategy / MRP policy	Cabinet for approval by Full Council	Annually before the start of the year
Treasury Management Strategy / Annual Investment Strategy / MRP policy – mid year report	Cabinet	Mid year
Treasury Management Strategy / Annual Investment Strategy / MRP policy – updates or revisions at other times	Cabinet for approval by Full Council	Periodically
Annual Treasury Outturn Report	Cabinet	Annually by 30th September after the end of the year
Treasury Management Monitoring and Performance Reports	Cabinet and Audit Committee	Quarterly Quarterly
Treasury Management Practices	Cabinet for approval by Full Council	Annually
Scrutiny of Treasury Management Strategy	Cabinet (and Audit Committee	Annually

6. This mid-year report has been prepared in compliance with CIPFA's Code of Practice, and covers the following:

- An economic update for 2019/20;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure (prudential indicators);
- A review of the Council's investment portfolio for 2019/20;

- A review of the Council's borrowing strategy for 2019/20;
- A review of any debt rescheduling undertaken during 2019/20;
- A review of compliance with Treasury and Prudential Limits for 2019/20.
- Revised Treasury and Prudential Limits for 2019/20 to 2021/22.

7. There have been no changes to the approved Treasury Management and Investment Strategies for the 6 months up to 30th September 2019 – updated Treasury Management Practices (TMP's) were approved by the cabinet on 30th October 2019.

Economic update

8. The first half of 2019/20 has seen UK **economic growth** fall as Brexit uncertainty took a toll. In its Inflation Report of 1 August, the Bank of England was notably downbeat about the outlook for both the UK and major world economies. This mirrored investor confidence around the world which is now expecting a significant downturn or possibly even a recession in some developed economies. It was therefore no surprise that the Monetary Policy Committee (MPC) left Bank Rate unchanged at 0.75% throughout 2019, so far, and is expected to hold off on changes until there is some clarity on what is going to happen over Brexit.

Interest rate forecasts

9. The Council's treasury advisor, Link Asset Services, has provided the following forecast:

Link Asset Services Interest Rate View											
	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25
3 Month LIBID	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20
6 Month LIBID	0.80	0.80	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40
12 Month LIBID	1.00	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60
5yr PWLB Rate	1.20	1.30	1.50	1.60	1.70	1.70	1.80	1.90	2.00	2.00	2.10
10yr PWLB Rate	1.50	1.60	1.80	1.90	2.00	2.00	2.10	2.20	2.30	2.30	2.40
25yr PWLB Rate	2.10	2.30	2.40	2.50	2.60	2.70	2.70	2.80	2.90	3.00	3.00
50yr PWLB Rate	2.00	2.20	2.30	2.40	2.50	2.60	2.60	2.70	2.80	2.90	2.90

The Council's Capital Position (Prudential Indicators)

10. This part of the report updates:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

The Council's Capital Expenditure and Financing 2019/20

	2018/19 Actual £'000	**2019/20 Original Estimate £'000**	**2019/20 Current Estimate £'000**
Capital expenditure	43,395	44,816	43,976
Resourced by:			
• Capital receipts	0	4,800	1,653
• Capital grants & contributions	15,196	23,199	25,285
• Capital reserves + DRF	606	1,344	1,690
Capital Expenditure to be financed from borrowing	**27,593**	**15,473**	**15,348**

11. The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). 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 unfinanced capital expenditure, and prior years' unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

12. 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.

13. Reducing the CFR – the Council's underlying borrowing need (CFR) is not allowed to rise indefinitely. 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.

14. 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).

18. The Council's 2019/20 MRP Policy (as required by CIPFA Code of Practice on Treasury Management) was approved by Council as part of the Treasury Management Strategy Report for 2019/20 on 14th February 2019.

19. The Council's CFR for the year is shown below, and represents a key prudential indicator.

CFR	**2018/19 Actual £'000**	**2019/20 Original Estimate £'000**	**2019/20 Current Estimate £'000**
Opening balance	325,241	337,698	338,543
Add unfinanced capital expenditure (Section 5.1)	27,593	15,473	15,348
Less MRP/Set aside receipts	(9,291)	(10,080)	(9,951)
Adjustment re: finance lease			
Closing balance	**338,543**	**343,091**	**343,940**

The borrowing activity is constrained by prudential indicators for net borrowing and the CFR, and by the authorised limit.

20. 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 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. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2019/20. The following table highlights the Council's net borrowing position against the CFR. This shows the Council is complying with this prudential indicator as projected net borrowing is less than the CFR.

	2018/19 Actual £'000	**2019/20 Original Estimate £'000**	**2019/20 Current Estimate £'000**
External Debt (Gross)	281,770	281,304	285,804
Less Investments	(55,100)	(61,000)	(61,000)
Net Borrowing Position	226,670	220,304	224,804
CFR	338,543	343,091	343,940

21. The authorised limit – the authorised limit is the "affordable borrowing limit" required by Section 3 of the Local Government Act 2003. The Council does not have the power to borrow above this level.

22. 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.

	2018/19 Actual £'000	2019/20 Original Estimate £'000	2019/20 Current Estimate £'000
Authorised Limit	373,725	380,994	393,940
Operational Boundary	353,725	360,994	373,940
Gross Borrowing *	281,770	281,304	285,804

* Total maximum long term and short term

23. This report confirms that during the first 6 months of 2019/20 Council has maintained gross borrowing within the Authorised Limit.

Investment Portfolio 2019/20

24. In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. As shown by forecasts in section 4.2, it is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the current 0.75% Bank Rate. The continuing potential for a re-emergence of a Eurozone sovereign debt crisis, and its impact on banks, prompts a low risk and short term strategy. Given this risk environment and the fact that increases in Bank Rate are likely to be gradual and unlikely to return to the levels seen in previous decades, investment returns are likely to remain low.

25. <u>It is confirmed</u> that the approved limits within the Annual Investment Strategy have not been breached during the first six months of 2019/20.

26. The Council's budgeted investment return for 2019/20 has been set at £300k which is a reflection of the low level of returns anticipated on investments.

27. The Treasury Management Strategy Statement (TMSS) for 2019/20, which includes the Annual Investment Strategy, sets out the Council's investment priorities as being:

- Security of Capital
- Liquidity

28. There has been no change in the Council's Investment Strategy aims from those approved on 14th February 2019. The aim continues to be to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. In the current economic climate, it is considered appropriate to keep an adequate level of investments which can be instantly accessed to cover short term cash flow needs. The Council also seeks out value where available in significantly higher rates in periods up to 12 months with approved institutions that meet the Council's stringent credit rating assessment.

29. Investment rates available have continued at historically low levels. The average level of funds available for investment purposes during the period was affected by the timing of precept payments, receipt of grants and progress on the Capital Programme.

Investment performance to the 30th September 2019

30. The Council held £57.3m of investments as at 30th September 2019 (£55.1m at 31 March 2019) and the investment portfolio yield for the first six months of the year is 0.73% against a benchmark 0.66%. The Council has outperformed the benchmark by 7 basis points. The benchmark for funds managed in-house is the 3 month LIBID uncompounded rate which is the most realistic comparison rate as advised by our treasury management consultants.

A full list of investments held as at 30th September 2019 is provided in Appendix 1.

Investment counterparty criteria and proposed amendments

31. The current investment counterparty criteria approved by Members earlier this year are detailed in Appendix 3 of this report.

32. The Current Investment Policy to allow for a maximum investment of £20m with F1 rated institutions. Currently classified as F1 by the Fitch credit reference agency are banks such as Lloyds Bank, Barclays Bank and Santander UK plc.

Borrowing

33. The Council's agreed Strategy in relation to borrowing is set out in the Treasury Management Strategy Report as approved by Council. This strategy outlined that consideration would be given to entering into new external borrowing if PWLB (or money market) rates became more favourable.

34. During 2019/20 the Council has, to date, entered into the following loan arrangements with the PWLB:

Date	Amount of Loan £'000	Type	Interest Rate %	Term of Loan (Yrs)
29/8/19	10,000	Maturity Loan	1.70	49.5

The loans are used to fund capital expenditure on assets including the 21st Century Schools Programme and Regeneration.

Borrowing in advance of need

35. The Council has not borrowed in advance of need during the six month period ended 30th September 2019. Members should note that the total external debt projection for 31st March 2020 is as follows:

	£'000
Public Works Loans Board (PWLB)	221,804
Market Loans	62,500
WG Town Centre Loan	1,500
Total	**285,804**

Debt Rescheduling

36. Debt rescheduling opportunities have been non-existent during 2019/20 due to the penalties involved in entering into such arrangements.

Compliance with Treasury and Prudential Limits

37. It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's original approved Treasury and Prudential Indicators (affordability) limits were included in the approved Treasury Management Strategy Statement as reported to Council on 14th February 2019.

38. During the financial year to date, the Council has operated within the Treasury Limits and Prudential Indicators set out in the Treasury Management Strategy Statement and in compliance with the Treasury Management Practices. The Prudential and Treasury Indicators for 2019/20 onwards have been revised and are presented in Appendix 2.

Financial Impact

39. All relevant financial information is provided in the body of the report.

Integrated Impact Assessment

40. There is no requirement to undertake an Integrated Impact Assessment as this report is for information purposes.

Valleys Communities Impacts

41. No implications

Workforce Impacts

42. There are no workforce impacts arising from this report.

Legal Impacts

43. There are no legal impacts arising from this report.

Risk Management

44. There are several risks associated with the treasury management activities. These include interest rate fluctuations, counter party investment, international economic and political etc. The treasury management strategy is included within the Council's Corporate Risk Register.

Consultation

45. There is no requirement under the Constitution for external consultation on this item.

Recommendations

46. It is recommended that Members:

    Note the Treasury Management activities to date this financial year, and how they relate to the proposed activities within the original 2019/20 Treasury Management Strategy and Annual Investment Strategy Statements.

Reason for Proposed Decision

47. To comply with requirements of the Code of Practice on Treasury Management.

Appendices

48. Appendix 1 – Investment Position as at 30th September 2019
Appendix 2 – Prudential Indicators
Appendix 3 – Specified Investments - Current Criteria

List of Background Papers

49. Link Asset Services Mid-year Reporting Template
Investment and Borrowing Records 2019/20

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Appendix 1

Investment Position as at 30th September 2019

Borrower	Maturity	Rate %	Total £'000
Banks and Building Societies			
Lloyds Banking Group	32 day notice	0.95	5,000
Other Local Authorities			
Blaenau Gwent CBC	21-Oct-19	0.80	3,000
Plymouth City Council	21-Oct-19	0.85	5,000
Uttlesford District Council	01-Nov-19	0.76	1,000
Flintshire CBC	04-Oct-19	0.78	4,000
Thurrock Borough Council	05-Nov-19	0.70	5,000
London Borough of Barking & Dagenham	25-Oct-19	0.73	3,000
Telford & Wrekin Council	28-Oct-19	0.72	3,000
Telford & Wrekin Council	01-Nov-19	0.73	5,000
Babergh District Council	25-Nov-19	0.65	3,000
Dudley Metropolitan BC	31-Dec-19	0.72	2,700
Call Deposit			
DMO		0.50	13,700
Santander		0.25	3,900
Total			**57,300**

Appendix 2

PRUDENTIAL INDICATORS

PRUDENTIAL INDICATORS	2018/19 Actual	2019/20 Original Estimate	2019/20 Revised Estimate	2020/21 Estimate	2021/22 Estimate
	£'000	£'000	£'000	£'000	£'000
Capital Expenditure	43,395	44,816	43,976	64,637	28,782
Capital Financing Requirement	338,543	343,091	343,940	345,346	345,716
Ratio of financing costs to net revenue stream	6.91%	7.31%	7.27%	7.09%	7.23%

Appendix 2

PRUDENTIAL INDICATORS

TREASURY MANAGEMENT INDICATORS	2018/19 Actual	2019/20 Original Estimate	2019/20 Revised Estimate	2020/21 Estimate	2021/22 Estimate
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Authorised Limit for External Debt:					
Borrowing and other long term liabilities	373,725	374,757	393,940	395,346	395,716
Operational Boundary for External Debt:					
Borrowing and other long term liabilities	353,725	354,757	373,940	375,346	375,716
External Debt (Gross)	281,771	282,804	285,804	293,598	299,597
Less Investments	(55,100)	(61,000)	(61,000)	(61,000)	(61,000)
Net Borrowing Position	**226,671**	**221,804**	**224,804**	**237,598**	**238,597**

Appendix 2

PRUDENTIAL INDICATORS

	2019/20 limit £'000
Upper Limit on Fixed Interest Rate Exposure	393,940
Lower Limit on Fixed Interest Rate Exposure	
Upper Limit on Variable Rate Exposure	196,970
Lower Limit on Variable Rate Exposure	
Upper Limit for Total Principal Sums Invested for Over 364 Days (per maturity date)	£25m

Maturity Structure of Fixed Rate Borrowing During 2018/19	**2018/19 Actual**	**2019/20 Estimate**		
	%	**%**	**Upper Limit %**	**Lower Limit %**
Under 12 months	2	3	15	0
12 months to 2 years	4	0	15	0
2 to 5 years	6	6	40	0
5 to 10 years	0	0	60	0
10 years and above	88	91	100	15

Appendix 3

Specified Investments Criteria

	Minimum 'High' Credit Criteria	Funds Managed	Max Amount	Max Duration
Term deposits				
Term deposits - Debt Management Office	N/A	In-house	Unlimited	1 year
Term deposits – local, police and fire authorities	N/A	In-house	£10m	1 year
Term deposits – Nationalised & Part Nationalised UK banks/Building Societies	Fitch short-term rating F1+, F1	In-house	£20m	1 year
Term deposits – UK banks/Building Societies	Fitch short-term rating F1+	In-house	£20m	1 year
Term deposits – UK banks/Building Societies	Fitch short-term rating F1	In-house	£15m	6 months or 185 days
Callable deposits				
Callable deposits – Debt Management Agency deposit facility	N/A	In-house	Unlimited	
Callable deposits – Nationalised & Part Nationalised UK banks/Building Societies	Fitch short-term rating F1+, F1	In-house	£20m	
Callable deposits – Nationalised & Part Nationalised UK banks/Building Societies	Fitch short-term rating F2	In-house	£10m	
Callable deposits - UK banks/Building Societies	Fitch short-term rating F1+ or F1	In-house	£15m *	
Term deposits – non UK banks	Fitch short-term rating F1+	In-house	£5m	6 months or 185 days

* Where necessary this limit may be temporarily exceeded with the Authority's bankers only.