Rotther District Council **Agenda Item: 7.2**

Report to	-	Audit and Standards Committee
Date	-	10 December 2018
Report of the	-	Executive Director
Subject	-	Treasury Management Update Report

Recommendation: It be **RESOLVED**: That the report be noted.

Assistant Director Resources: Robin Vennard

Introduction

1. Council approved the 2018/19 Investment Strategy in February this year (Minute Reference C17/63). The investment strategy requires regular reports to be presented to this Committee on the Council's treasury management activities. In managing its treasury management activities, the Council follows the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017).

2. Treasury Management covers two main areas:-

    i. The management of day to day cash flows by way of short term investing and borrowing. Longer term investment opportunities may arise depending on cashflow requirements.
    ii. Management of the Council's long term debt portfolio which is used to finance capital expenditure that cannot be immediately funded by internal resources (e.g. by Capital Receipts).

3. The following paragraphs describe the recent investment activity and the level of investment returns currently being generated.

Investment Portfolio 2018/19

4. 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. 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 with the Bank rate now at 0.75%. The Council's cash levels and cash flow profiles, as well as restrictions on maximum deposit duration, contribute to a low risk and short-term strategy. Given this risk averse environment, investment returns are likely to remain low. The Council's treasury advisors, Link Asset Services, latest financial commentary is shown at Appendix A.

5. The Council held £31m of investments as at 31 October 2018 and the investment portfolio yield to 31 October 2018 was £218,107. The average rate of return is 1.47%

The following table shows the current investments:

Deposit with	Type of account	Maturity Date	Amount	Interest rate %
Nat West	Deposit	10/05/2019	£2,000,000	0.75
Lloyds	Deposit	21/12/2018	£2,000,000	0.75
Lloyds	Deposit	02/07/2019	£1,500,000	1.00
Lloyds	Deposit	05/07/2019	£1,000,000	1.00
Lloyds	Deposit	16/08/2019	£1,000,000	1.05
Santander	31 Day Notice		£1,642	0.40
Santander	Deposit	06/02/2019	£3,000,000	0.90
Santander	Deposit	18/02/2019	£1,195,000	0.90
Barclays	Call Account		£1,057	0.05
Bank of Scotland	Deposit	18/19/2019	£3,000,000	1.00
Bank of Scotland	32 Day Notice		£2,300,000	0.82
Bank of Scotland	Call Account		£36	0.40
Lloyds - general	Call Account		£6,107,829	0.65
HERMES Property Fund	Long Term		£2,999,998	4.86 Est
Local Authority Property Fund	Long Term		£5,000,000	4.47
Total Invested			**£31,860,563**	

6. The Assistant Director Resources (the Council's Chief Financial Officer) confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2018/19.

7. If the Hermes Property fund achieves the estimated return highlighted above, together with the other Council investments, the return for 2018/19 should be in the region of £410,000.

Investment Counterparty Criteria

8. The current investment counterparty criteria selection approved in the Treasury Management Strategy Statement is meeting the requirement of the treasury management function.

Capital Programme

9. A major part of the Council's Treasury Management Strategy concerns the Capital Programme, how it is funded and the impact this has on our taxpayers.

Financing of the Capital Programme

10. The table below draws together the main strategy elements of the capital expenditure plans, highlighting the original supported and unsupported elements of the capital programme and the expected financing arrangements of

this capital expenditure. Any borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). Any direct borrowing need may also be supplemented by maturing debt and other treasury requirements. The profile of the borrowing shown below may accelerate depending on the demands of the Council's regeneration plans within the Property Investment Strategy.

Rother District Council
Capital Programme Summary

	2018/19 Estimated Outturn £ (000)	2019/20 Projected Budget £ (000)	2020/21 Budget £ (000)
Total	**8,550**	**12,738**	**20,130**
Funded By:			
Capital Receipts	1,345	1,683	
Grants and contributions	1,329	90	
Borrowing	4,338	10,000	20,000
Capital Expenditure charged to revenue	1,538	965	130
Total Funding	**8,550**	**12,738**	**20,130**

Capital Financing Requirement and Borrowing

11. The Council's CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the Public Works Loan Board (PWLB) or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The CFR will increase each year by the amount of capital expenditure yet to be financed and is reduced by the amount that the Council sets aside for the repayment of borrowing.

12. £1.091 million of the CFR balance for 2018/19 of £5.429 million represents an "Item A" adjustment dating back to 2004: this is the agreed historic amount on which it is not necessary to provide the annual Minimum Revenue Provision (MRP) for repayment of debt. MRP would be payable for any capital expenditure financed from loan in the future.

Limits to Borrowing Activity

13. To ensure the Council acts reasonably when entering into borrowing, the first key control over the treasury activity is a Prudential Indicator (PI) to ensure that over the medium-term, net borrowing (borrowings less investments) will only be for a capital purpose. Net external borrowing should not, except in the short-term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2018/19 and next 2 financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need, which will be adhered to if this proves prudent.

14. The Assistant Director Resources reports that no difficulties are envisaged for the current or future years in complying with this PI.

15. A further PI controls the overall level of borrowing. This is the Authorised Limit (AL), which represents the limit beyond which borrowing is prohibited and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short-term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under Section 3 (1) of the Local Government Act 2003.

16. The Operational Boundary links directly to the Council's estimates of the CFR and estimates of other cash flow requirements. This indicator is based on the same estimates as the AL, reflecting the most likely but not worst case scenario, but without the additional headroom included in the AL.

Authorised limit	**2018/19 Estimate £'000**	**2019/20 Estimate £'000**	**2020/21 Estimate £'000**
Debt	26,600	35,400	56,300
Other long term liabilities	0	0	0
Total	**26,600**	**35,400**	**56,300**

Operational boundary	**2018/19 Estimate £'000**	**2019/20 Estimate £'000**	**2020/21 Estimate £'000**
Debt	24,000	32,000	51,000
Other long term liabilities	0	0	0
Total	**24,000**	**32,000**	**51,000**

17. The maximum cash outflow in a month, plus potential short-term borrowing is estimated to be around £24m and this leads to the Operational Boundary quoted above.

Conclusion

18. The Council's current treasury management and investment strategies remain robust in managing the Council's cash funds. The economic outlook remains difficult for a net investor such as the Council and supports the Council's financial strategy to reduce reliance on investment returns.

Malcolm Johnston
Executive Director

Risk Assessment Statement
There are no direct risks arising from this report. Failure to follow the Council's investment strategy could increase the risk of financial loss.

Link Asset Services – Weekly Economic Update 29 November 2018

Country	Event	Market Forecast	Previous
UK	Net Consumer Credit/Mortgage Approvals (Oct)	+£0.9bn/+64k	+£0.8bn/+65,269
EZ	EC Business and Consumer Survey (Nov)	109.0	109.8
GER	CPI (Nov prov)	-0.2% (+1.9%)	+0.1% (+2.4%)
US	Personal Income / Spending (Oct)	+0.5% / +0.6%	+0.2% / +0.4%
US	Core PCE Deflator (Oct)	+0.2% (+1.9%)	+0.2% (+2.0%)
US	Pending Home Sales (Oct)	+0.9%	+0.5%
US	November FOMC Minutes Released		
JAP	Retail Sales (Oct)	+1.2% (+3.5%) (ACTUAL)	+0.1% (+2.2%)

Latest News

The FTSE 100 stuttered to a 0.18% dip as Brexit worries continue to weigh on the markets, with banking and housebuilder stocks easing amid the no deal Brexit warnings. European markets steadied, but still posted minor losses, as trade war fears eased as the prospect of a G20 meeting between the US and China improved. Wall Street posted strong gains on Fed Chair, Jerome Powell hinting that there could be fewer US rate hikes ahead, easing investor concerns. He said that rates were "just below" neutral level. The three markets spiked to gains of 2.3-2.95% on the comment, bolstering moves on the hopes of Sino-US trade talks this weekend. Asia/Pacific markets have broadly registered moderate gains as they tracked Wall Street higher. The Nikkei hit a three week high and Chinese stocks improved, but the Hang Seng bucked the trend with a 0.8% fall.

UK

There were no key economic data releases yesterday. The Government's analysis of the economy under Brexit indicates that the UK will suffer some shrinkage of around 3.9% over the coming fifteen years under Mrs May's plan, compared to remaining in the EU, but a no deal Brexit would be a lot worse, with a hit of 9.3%. That said, the economy will continue to expand in this and all Brexit scenarios, but all indicate that the economy will be smaller outside of the EU. The BoE also warned that a disorderly "no deal" Brexit scenario would have a greater impact on the economy than the 2008 crisis, suggesting that there could be an economy crash, with GDP to fall by 8% and unemployment to rise to 7.5%. With the Government vote on the deal taking place on December 11th expect the rhetoric surrounding Brexit to become like that ahead of the referendum, a frenzy from both sides of the argument.

Eurozone

The German Gfk measure of consumer confidence eased to 10.4 for December, which was marginally lower than forecast. It is the lowest reading for eighteen months and comes amid persistent concerns over trade with the US, as well as the ongoing Brexit negotiations.

US

The second estimate of Q3 GDP growth was unchanged at 3.5%, confirming slowing from 4.2% in Q2, which was the highest since Q3 2014. The figures showed upward revisions to non-residential fixed investment and private inventory investment were offset by downward revisions to personal consumption expenditure and state/local government spending. The advance goods trade deficit widened by $1bn in October, to $77.25bn

Asia/Pacific

Japanese retail sales beat expectations, picking up at a rate of 1.2% last month, pushing annual growth to a ten month high 3.5%. The largest gains were seen in fuel sales, while motor vehicle sales also accelerated, but general merchandise sales declined further.

Gilts / Debt

It was another mixed session on the gilt market yesterday with shorter dated gilts being purchased and pushing yields down by 1-3 basis points, with medium to longer term issuance sold, generating increases in yields of 1-2 basis points, as investors react to the comments from the Government and Bank of England over Brexit.

Investment

The November MPC meeting delivered the expected no change vote with a unanimous 9-0 vote. The Inflation Report suggested that inflation could breach the target level within the three year time horizon and later comments that the budget measures had the "potential to be significant" will add to the view that the Bank has its finger on the rate trigger, but has been restrained by the impasse over Brexit. The turmoil over the PMs Brexit deal saw interest rate expectations curbed, and comments about the future state of the economy from the various Brexit scenarios has dented them once more. A February rate hike is now marked at a just above 10% chance, while May prospects have been slashed to 34%. August, September and November chances are priced at around 50-55%. The volatility in expectations remains and if a Brexit deal can be brokered that meets the approval of Parliament, and a disorderly exit is avoided, the Bank of England looks primed to raise rates, but at present with political risks high, and a deal sign off still unlikely, the interest rate outlook remains misty. Clients with lower returning Call Accounts and Money Market Funds may want to look at the shorter dated deposits offered through the Agency Treasury Service, which provide short dated liquidity options at reasonable rates. Please contact your Relationship Team or the Agency Treasury team if you wish to discuss.

Market Rates

	Equities				Currencies			Commodities		Risk Indicators	
	FTSE 100	DOW	NIKKEI	DAX	£/$	€/£	€/$	Brent	Gold	VFTSE	MOVE
Level	7,004.52	25,366.43	22,262.60	11,298.88	1.2841	1.1278	1.1386	58.18	1,225.92	17.7110	50.7621
Change	-0.18%	2.50%	0.39%	-0.09%	0.61%	-0.08%	0.68%	-3.89%	0.51%	13.08%	-0.93%

Interest Rates												Average LIBID / LIBOR Rates		
O/n	1W	1M	3M	6M	9M	12M	24M	36M	48M	60M	SONIA	7D LIBID	3M LIBID	3M LIBOR
0.45	0.45	0.75	0.85	0.95	1.05	1.1	1.4	1.5	1.6	1.6	0.7018	0.47%	0.63%	0.76%

PWLB (Includes Certainty Rate)					Forward Rates			
1y	5y	10y	25y	50y	3M/3M FWD	3M/6M FWD	3M/9M FWD	6M/12M FWD
1.53	1.74	2.17	2.86	2.74	0.89	0.94	0.99	1.14

Interest Rate Forecasts

Bank Rate	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20
Link	0.75%	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%
Cap Econ	0.75%	0.75%	1.00%	1.25%	1.50%	1.50%	1.75%	1.75%
5Y PWLB RATE								
Link	2.00%	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%
Cap Econ	2.00%	2.00%	2.20%	2.40%	2.70%	2.70%	2.80%	2.80%
10Y PWLB RATE								
Link	2.50%	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%
Cap Econ	2.30%	2.40%	2.60%	2.80%	3.10%	3.10%	3.10%	3.10%
25Y PWLB RATE								
Link	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%
Cap Econ	2.80%	3.00%	3.10%	3.30%	3.60%	3.50%	3.50%	3.40%
50Y PWLB RATE								
Link	2.70%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%
Cap Econ	2.70%	2.80%	2.90%	3.20%	3.40%	3.40%	3.40%	3.40%

Appendix B

Approved countries for investments as at 23.11.2018

Since publication of the Treasury Management Strategy and annual Investment Strategy in February 2018, the approved list of countries has changed as detailed below.

Based on lowest available rating:

AAA

- Australia
- Canada
- Denmark
- Germany
- Hong Kong
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland
- USA

AA+

- Finland

AA

- Abu Dhabi (UAE)
- France
- U.K.

AA-

- Belgium
- Qatar