

<b>AUDIT COMMITTEE</b>	AGENDA ITEM No. 6
<b>24 SEPTEMBER 2018</b>	PUBLIC REPORT

Committee Member(s) responsible:	Resources portfolio holder, Cllr Seaton	
Contact Officer(s):	Peter Carpenter, Interim Corporate Director: Resources Kirsty Nutton, Head of Corporate Finance	☎ 452520 ☎ 384590

## TREASURY MANAGEMENT MID YEAR UPDATE

<b>R E C O M M E N D A T I O N S</b>	
<b>FROM : Peter Carpenter</b> , Acting Corporate Director: Resources	<b>Deadline date : N/A</b>
<p>Audit Committee is asked to</p> <ol style="list-style-type: none"> <li>1. To review current performance against the Prudential Indicators as approved in the Treasury Management Strategy (TMS) contained in the Medium Term Financial Strategy (MTFS).</li> <li>2. To note as outlined in Cabinet Reports for Tranche 1, it is expected that the capital programme will reduce in future months due to re-profiling of the programme to a more deliverable level of £100m, however exact details are to be confirmed.</li> </ol>	

### 1. ORIGIN OF REPORT

- 1.1 The Treasury Management in the Public Services: Code of Practice 2017 recommends that Members receive reports on its treasury management policies, practices and activities, including an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close.
- 1.2 The annual strategy is approved by Council as part of the MTFS. The original strategy was approved on 7 March 2018. The final performance against the revised strategy will be reported to Audit Committee in July 2019 alongside the Statement of Accounts. This report forms the mid-year review against the Prudential Indicators as set out in the TMS.

### 2. PURPOSE AND REASON FOR REPORT

- 2.1 To report current performance and the forecast outturn position against the Prudential Indicators in the strategy.
- 2.2 This is in accordance with the Committees' Terms of Reference – 2.2.2.15 To consider the Council's arrangements for corporate governance and agreeing necessary actions to ensure compliance with best practice.

### 3. TIMESCALE

Is this a Major Policy Item / Statutory Plan?	<b>NO</b>	If Yes, date for relevant Cabinet Meeting	N/A
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### 4. TREASURY MANAGEMENT STRATEGY PRUDENTIAL INDICATORS

- 4.1 The Prudential Code underpins the system of capital finance. Local authorities determine their own programmes for capital investment in long term and current assets that are central to the delivery of quality local public services. Prudential indicators are developed as part of the annual MTFS process to ensure that:

- a) Capital investment plans are affordable;
- b) All external borrowing and other long term liabilities are within prudent and sustainable levels; and
- c) Treasury management decisions are taken in accordance with professional good advice.

- 4.2 The 2018/19 Prudential Indicators are shown in Appendix 1. The Council's performance to date and forecast performance are all within the limits set in the MTFS.
- 4.3 The Council has continued to operate a restrictive lending list due to the continued economic uncertainty. Surplus cash is only invested for short periods with Barclays, Bank of Scotland (part of the Lloyds Banking Group) and the Churches, Charities and Local Authorities (CCLA) money market fund. The Council also invests with other Local Authorities and the Debt Management Office (DMO).
- 4.4 The Council forecasts to borrow to fund the capital investment programme. The Council's approach is for loans to be arranged at fixed interest rates to achieve budget certainty and over varying periods to fit in with the Councils debt maturity profile. However, due to cash flow timings, the Council's borrowing has actually reduced by £3m to date.
- 4.5 The Bank of England Monetary Policy Committee increased the Base Rate from 0.50% to 0.75% in August 2018. This was the second interest rate rise since August 2016. This increase is anticipated to have an impact on the cost of any new borrowing taken after this date as well as on income received from investing surplus cash balances.

## **5. CONSULTATION**

- 5.1 The Council's Prudential Indicators and Treasury Management Strategy 2018/19 - 2020/21 have undergone full consultation, and been through the scrutiny process, as it forms part of the Annual MTFS.
- 5.2 The Council continues to liaise with its treasury advisors, Link Asset Services.

## **6. ANTICIPATED OUTCOMES**

- 6.1 As set out in the report.

## **7. REASONS FOR RECOMMENDATIONS**

- 7.1 This report is given to the Committee to review performance against the Prudential Indicators in the TMS set in the MTFS.

## **8. ALTERNATIVE OPTIONS CONSIDERED**

The Treasury Management Strategy 2018/19 – 2020/21 is required to be prepared in accordance with the Treasury Management in the Public Services: Code of Practice 2017. This report sets out the performance against the associated prudential indicators. The options are therefore limited.

## **9. IMPLICATIONS**

- 9.1 To provide the Committee the opportunity to review current performance against the revised Prudential Indicators.

### **Legal Implications**

9.2 Treasury Management activities have to conform to the Local Government Act 2003, the Local Authorities (Capital; Finance and Accounting) (England) Regulations 2003 (SI 2003/3146), which specifies that the Council is required to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice and also the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (SI 2008/414), which clarifies the requirements of the Minimum Revenue Provision guidance.

## **10. BACKGROUND DOCUMENTS**

(Used to prepare this report, in accordance with the Local Government (Access to Information) Act 1985)

- The Prudential Code for Capital Finance in Local Authorities –2017 Edition, CIPFA; and
- Treasury Management in the Public Services, Code of Practice and Cross-Sectoral Guidance Notes – 2017 Edition, CIPFA

## **11. APENDICES**

- Treasury Management Strategy – Prudential Indicators – Forecast Outturn as at 31 August 2018.

## Treasury Management Strategy – Prudential Indicators – Forecast Outturn as at August 2018

The Prudential Code for Capital Finance in Local Authorities provides a framework for local authority capital finance to ensure that:

- (a) capital expenditure plans are affordable,
- (b) all external borrowing and other long term liabilities are within prudent and sustainable levels;
- (c) treasury management decisions are taken in accordance with professional good practice.

In taking decisions in relation to (a) and (c) above, the local authority is accountable by providing a clear and transparent framework.

The Code requires the Council to set a range of Prudential Indicators for the forthcoming financial year and at least the following two financial years. The Council has set out indicators for the next three financial years in line with setting a three year budget.

In the current financial year to date, the Council has operated within the treasury limits and Prudential Indicators set out in the Council's Revised Annual Treasury Management Strategy.

The actual and forecast outturn, compared to those contained in the MTFS for the Prudential Indicators for this financial year are detailed below. The indicators include the Invest to Save schemes however the costs of borrowing associated with these schemes will be offset by the income generated by these projects. All performance is within the limits.

### 1. Indicator 1: Capital Expenditure

This indicator is the estimated capital expenditure for the year based on the Capital Programme for that period.

<b>Capital Expenditure</b>	<b>2018/19 Indicator £m</b>	<b>2018/19 Actual at 31.08.2018 £m</b>	<b>2018/19 Forecast Outturn £m</b>
Capital Expenditure	115.3	30.6	115.7
Invest to Save	43.4	0.3	18.0
<b>Total</b>	<b>158.7</b>	<b>30.9</b>	<b>133.7</b>

### 2. Indicator 2: Capital Financing Requirement (CFR)

The CFR measures the Council's underlying need to borrow money in the long term for capital purposes. Any capital expenditure which has not immediately been paid for will increase the CFR.

<b>Capital Financing Requirement</b>	<b>2018/19 Indicator £m</b>	<b>2018/19 Actual at 31.08.2018 £m</b>	<b>2018/19 Forecast Outturn £m</b>
CFR b/fwd	555.4	540.1	540.1
Underlying Need to Borrow	51.6	15.6	73.5
Underlying Need to Borrow - Invest to Save	43.4	0.3	18.0
Repayment of debt - Minimum Revenue Provision	(13.1)	(14.5)	(14.5)
Repayment of loan – capital receipt	(1.0)	(1.0)	(1.0)
<b>Total CFR C/fwd</b>	<b>636.3</b>	<b>540.5</b>	<b>616.1</b>

### 3. Indicator 3: Actuals and Estimates of the Ratio of Financing Costs to Net Revenue Budget

The Council must estimate the proportion of the revenue budget, which is taken up in financing capital expenditure i.e. the net interest cost and to make provision to repay debt.

<b>Ratio of net financing costs to net revenue stream</b>	<b>2018/19 Indicator</b>	<b>2018/19 Actual at 31.08.2018</b>	<b>2018/19 Forecast Outturn</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Total Ratio	7.4%	3.7%	5.0%

### 4. Indicator 4: Proportion of Gross Debt to the Capital Financing Requirement (CFR)

This indicator shows the proportion of the Council's external borrowings (Gross Debt) against the CFR. In order to ensure that borrowing levels are prudent over the medium term and only for capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2017/18) plus the estimates of any additional capital financing requirement for the current (2018/19) and the next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure.

<b>Proportion of Gross Debt to the CFR</b>	<b>2018/19 Indicator</b>	<b>2018/19 Actual at 31.08.2018</b>	<b>2018/19 Forecast Outturn</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Gross Debt	558.8	451.3	532.4
CFR	636.3	540.5	616.1
<b>% of Gross Debt to CFR</b>	<b>87.8%</b>	<b>81.2%</b>	<b>86.4%</b>

This indicator shows that the Council is maintaining an under-borrowed position. This means that the capital borrowing need (the CFR), is not fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow is being used. This strategy continues to be prudent as investment returns remain low and counterparty risk continues variable.

### 5. Indicator 5: The Operational Boundary

The Operational Boundary is a measure of the day to day likely borrowing for the Council. The code recognises that circumstances might arise when the boundary might be exceeded temporarily, but if this continues for a lengthy period then it ought to be investigated.

This indicator takes into consideration the capital programme over the life of the MTFS and the ability to phase the borrowing over this period. The indicator provides flexibility for the Council to take advantage of favourable interest rates in advance of the timing of the actual capital expenditure.

<b>Operational Boundary</b>	<b>2018/19 Indicator</b>	<b>2018/19 Actual at 31.08.2018</b>	<b>2018/19 Forecast Outturn</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Borrowing	659.7	416.6	495.6
Other Liabilities	36.8	34.7	34.7
<b>Total Operational Boundary</b>	<b>696.5</b>	<b>451.3</b>	<b>530.3</b>

## 6. Indicator 6: The Authorised Limit

The Authorised Limit represents the maximum amount the Council may borrow at any point in time in the year. It is set at a level the Council considers is “prudent”.

The indicator takes account of the capital financing requirement estimated at the start of each year, plus the expected net borrowing requirement for the year. This makes allowance for the possibility that the optimum time to do all borrowing may be early in the year.

The limits also incorporated margins to allow for exceptional short-term movements in the Council’s cash flow, bids from service departments to finance efficiencies, changes to the timing of capital payments and fluctuations in the realisation of capital receipts.

<b>Authorised Limit</b>	<b>2018/19 Indicator £m</b>	<b>2018/19 Actual at 31.08.2018 £m</b>	<b>2018/19 Forecast Outturn £m</b>
Borrowing	706.5	416.6	505.6
Other Liabilities	36.8	34.7	34.7
<b>Total Authorised Limit</b>	<b>743.3</b>	<b>451.3</b>	<b>540.3</b>

It is ultra vires to exceed the Authorised Limit so this should be set to avoid circumstances in which the Council would need to borrow more money than this limit. However, the Council can revise the limit during the course of the year. The forecast outturn is lower than the indicator as the Council does not currently anticipate borrowing in advance of need due to the additional cost of holding the funds until required.

## 7 Indicator 7: Fixed Interest rate exposure

This indicator places an upper limit on the total amount of net borrowing which is at fixed rates secured against future interest rate movements. The upper limit allows flexibility in applying a proportion of the investment portfolio to finance new capital expenditure. It also reflects a position where the majority of borrowing is at fixed rate which provides budget certainty with 100% of borrowing being at fixed rate. The upper limit for fixed interest rate exposure was set to allow for flexibility in applying a proportion of the investment portfolio to finance new capital expenditure. It also reflected a position where the majority of borrowing was at fixed rates to provide budget certainty.

<b>Upper limit for fixed rate exposure</b>	<b>2018/19 Indicator £m</b>	<b>2018/19 Actual at 31.08.2018 £m</b>	<b>2018/19 Forecast Outturn £m</b>
Upper Limit	669.7	416.6	505.6
% of fixed interest rate exposure	100%	100%	100%

## 8. Indicator 8: Variable interest rate exposure

This indicator places an upper limit on the total amount of net borrowing (borrowing less investment) which is at variable rates subject to interest rate movements. The intention is to keep the variable rate borrowing below 25% of the total gross borrowing (CFR). The limit is expressed as the value of total borrowing less investments.

<b>Upper limit for variable rate exposure</b>	<b>2018/19 Indicator £m</b>	<b>2018/19 Actual at 31.08.2018 £m</b>	<b>2018/19 Forecast Outturn £m</b>
Upper Limit	167.4	0.0	0.0
% of variable interest rate exposure	25%	25%	25%

The indicator for actual and forecast outturn is zero due to the current borrowing strategy of borrowing only at a fixed interest rate in the current economic climate of volatile interest rates. Borrowing at fixed interest rates provides budget certainty for the Council.

### Indicator 9: Maturity structure of borrowing

The prudential limits have been set with regard to the maturity structure of the Council's borrowing, and reflected the relatively beneficial long term rates that were expected to be available over the next few years. The borrowing that the Council has actually taken up to the end of August is £416.6m shown in the indicator below.

Period	Upper Limit Indicator	Actual at 31.08.2018	
	%	%	£m
Under 12 months*	40	6	27.0
1 – 2 years	40	9	38.0
3 – 5 years	80	4	16.1
6 – 10 years	80	4	15.7
Over 10 years	100	77	319.8
<b>Total Borrowing</b>			<b>416.6</b>

\* The borrowing for under 12 months includes £17.5m of Lenders Option Borrowers Option (LOBO) loans. Although the loans are due to mature in 23-35 years time, they are classed as loans repayable within the financial year due to LOBO's having a call-in date every 6 months.

### 9. Indicator 10: Total Investments for periods longer than 365 days

Authorities are able to invest for longer than 365 days excluding loans. This can be advantageous if higher rates are available. However it would be unwise to lend a disproportionate amount of cash for too long a period particularly as the Council must maintain sufficient working capital for its operational needs.

	2018/19 Indicator £m	2018/19 Actual at 31.08.2018 £m	2018/19 Forecast Outturn £m
Principal sums invested >364 days	10.0	0.0	0.0

This indicator reflects the Council's current lending policy of keeping investments short term for liquidity purposes. Also the Council has run down its cash balances as an alternative to new borrowing and does not have the available cash balances to invest for long periods.

This indicator was set at £10m to allow for the accounting treatment of the Local Authority Mortgage Scheme (LAMS) which was treated as capital expenditure, as a loan to a third party. The Council can confirm that these capital loans have now been fully returned.

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