



RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL

MUNICIPAL YEAR 2019 / 2020

COUNCIL

27th November 2019

2019/20 MID YEAR TREASURY MANAGEMENT STEWARDSHIP REPORT

REPORT OF THE DIRECTOR OF FINANCE AND DIGITAL SERVICES : Barrie Davies (01443) 424026

1.0 PURPOSE OF REPORT

- 1.1 The CIPFA Code of Practice on Treasury Management requires a Mid Year Review to be presented to Council. This report provides Members with information on:-
- The Council's Treasury Management activity during the first six months of 2019/20; and
 - Prudential and Treasury Indicators for the same period.
- 1.2 To approve the updated Treasury Management Policy Statement and Clauses (Appendix 1).

2.0 RECOMMENDATIONS

- 2.1 It is recommended that Members:
- 2.1.1 Note the content of this report; and
- 2.1.2 Approve the Treasury Management Policy Statement and Clauses (Appendix 1).

3.0 INTRODUCTION

- 3.1 This report meets the requirements of both the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities.
- 3.2 The Treasury Management function operates within the Treasury Management Strategy and Capital Strategy, both approved by Council on the 27th March 2019.
- 3.3 Treasury Management is defined as:
“The management of the organisation’s borrowing, 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.”
- 3.4 The Council sets a balanced budget to ensure that all planned expenditure is financed by various sources of income / reserves. Treasury Management is concerned with monitoring the cash flows of such income and expenditure and planning investments and borrowing prudently.
- 3.5 This report includes the following areas of treasury activity during the first six months of 2019/20:
- Economic background;
 - Borrowing activity and results;
 - Estimated and actual treasury position, treasury management and prudential indicators; and
 - Investment strategy, activity and results.

4.0 ECONOMIC BACKGROUND

4.1 General Economic Background

- 4.2 The Council’s investment income is subject to changes in short term interest rates. The level of the Bank Base Rate or ‘Bank Rate’ is one of the main determinants of the rate of interest the Council receives on its short-term investments. The Bank of England Monetary Policy Committee has maintained the Bank Rate at 0.75% throughout this financial year to date and, in its August 2019 Inflation Report, noted that the outlook for global growth has deteriorated a little, impacted by trade tensions between the US and China. The August Report also confirmed that the UK economic outlook would continue to depend significantly on the nature and timing of its withdrawal from the European Union.
- 4.3 In line with the outlook set out above, the UK economy has displayed a slowdown in growth, with the Office for National Statistics reporting a Quarter 2 growth rate of -0.2%. The latest statistics for the three months to August 2019 shows the unemployment rate at 3.9%, lower than a year earlier

(4.0%). Real wages (that is, after allowing for inflation), excluding bonuses increased by 2.0% during the year to August 2019.

- 4.4 The Consumer Price Index (CPI) fell to 1.7% in August 2019, from 2.0% in July 2019, and remained at 1.7% for September 2019. This rate is below the Bank of England’s target of 2%.
- 4.5 The majority of the Council’s borrowing is from the PWLB (Public Works Loans Board). Long-term borrowing rates are influenced by gilt yields and, in the first six months of this financial year, the cost of borrowing from PWLB had fallen to record lows. However, on 9th October 2019 HM Treasury raised PWLB interest rates by 1%, to restore interest rates to levels available in 2018, with the higher rate to apply to all new loans from this date.
- 4.6 PWLB maturity rates (certainty rate) during the first half of the financial year were as follows:

	5 years	10 years	20 years	50 years
Average	1.38%	1.66%	2.15%	2.07%
Highest	1.76%	2.10%	2.53%	2.41%
Lowest	1.00%	1.15%	1.66%	1.57%

- 4.7 Estimates of future rates are as follows:

	Base Rate	PWLB Maturity Rates			
		5 years	10 years	20 years	50 years
2019/20 (Act 6 mth Average)	0.75%	1.38%	1.66%	2.15%	2.07%
31/03/20 ¹	0.75%	2.20%	2.35%	2.80%	2.75%
31/03/21 ¹	0.75%	2.30%	2.55%	2.95%	2.90%

5.0 REGULATORY AND CODE OF PRACTICE UPDATES

- 5.1 In September 2019, Welsh Government issued a consultation on the statutory guidance on Local Government investments. The Welsh Government recognises that local authorities will hold investments for different purposes and therefore the proposed revised regulations make a distinction between investments held for treasury management purposes and those held for commercial purposes. The definition of investments is widened to include “all of the financial and non-financial assets a local authority has invested money into primarily or partially for the purpose of generating a surplus including investment property”. The revised guidance would be effective from April 2020.

¹ PWLB Maturity Rates (31/3/20 and 31/3/21) – includes the PWLB interest rate increase that was effective from 9th October 2019.

5.2 Included at Appendix 1 is an updated Treasury Management Policy Statement and Clauses. The Policy Statement and Clauses have been updated in line with the latest guidance including the CIPFA Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes. The Treasury Management Policy Statement defines the policies and objectives of the Council's treasury management activities.

6.0 BORROWING ACTIVITY AND RESULTS

6.1 The borrowing strategy for 2019/20, approved by Council in March 2019, reported that the Director of Finance and Digital Services, as Section 151 Officer (or in his absence the Deputy Section 151 Officer), under delegated powers, will take the most appropriate form of borrowing depending upon the prevailing interest rates at the time, and taking into account advice provided by our advisors.

6.2 In March, the borrowing requirement was estimated to be £44.0m based on the Capital Programme at that time. The borrowing requirement for 2019/20 has increased to £46.7m as at 30th September 2019. The increase is due to revised delivery timescales for projects, including the re-profiling of expenditure on school modernisation projects.

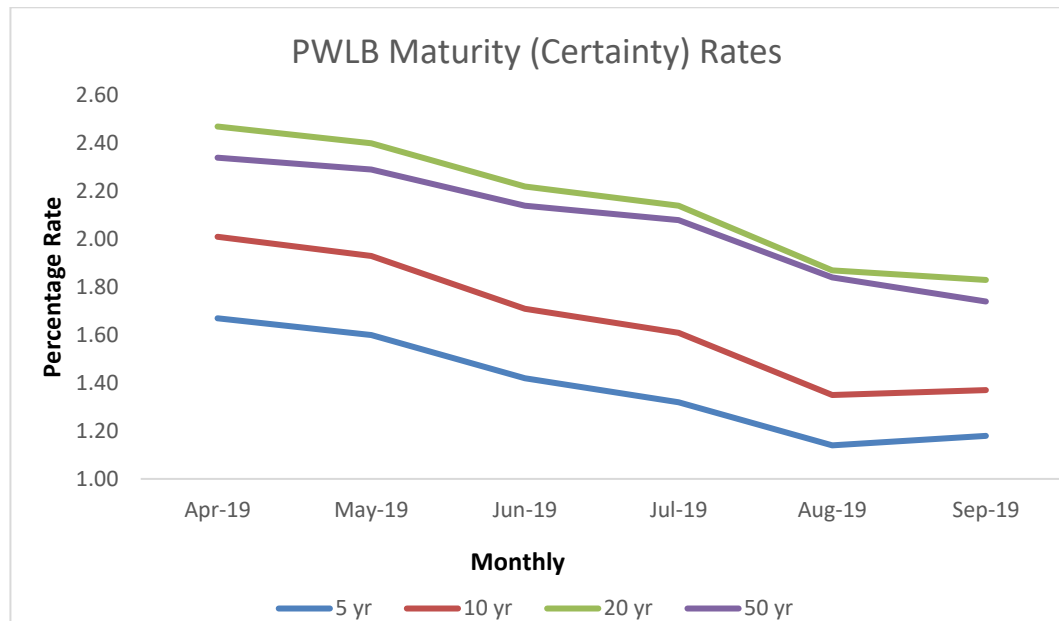
6.3 It was also reported that the Council would monitor prevailing PWLB rates for any opportunities to reschedule debt to generate savings. I can report that to the 30th September this financial year, the Council has not had a viable option to reschedule debt. Affordability and the cost of carry remained important influences on the Council's borrowing strategy. Whilst short-term borrowing was taken during the first half of 2019/20, the Council also took the opportunity, in line with advice, to take longer-term debt, to take advantage of favourable PWLB rates.

6.4 A breakdown of PWLB long term borrowing undertaken during the first six months of the year is set out below:

Date	Loan Type	PWLB Loan Amount	Period	Rate
		£M		%
5th July 2019	EIP(Certainty Rate)	30.000	15 years	1.41
5 th August 2019	EIP(Certainty Rate)	10.000	15 years	1.30
6 th August 2019	EIP(Certainty Rate)	10.000	15 years	1.25
29 th August 2019	EIP(Certainty Rate)	10.000	12.5 years	1.06
5 th September 2019	EIP(Certainty Rate)	20.000	12.5 years	1.00
Total		80.000		

The EIP rate refers to the half yearly equal instalments of principal repayments of the loan.

The graph below shows the changes in the longer term PWLB borrowing rates during the first six months:



- 6.5 In line with the above strategy, this Council has not borrowed in advance of need during the first 6 months of the year and has no current intention to borrow in advance during the remainder of 2019/20.
- 6.6 No variance is currently being projected for net capital charges, as at 30th September 2019, which have a budget for 2019/20 of £18.9m. This is being achieved despite the challenges faced with investment income and maintaining our low risk strategy.

7.0 CERTAINTY RATE

- 7.1 The “certainty rate”, whereby local authorities are able to access borrowing at 0.2% below published PWLB rates was available from HM Treasury again for this year. Authorities were required to provide an indication of their potential borrowing requirements for the next 3 years. This Council provided such information to HM Treasury and will continue to be able to access the discounted rate up to 31st October 2020.

8.0 ESTIMATED AND ACTUAL TREASURY POSITION AND PRUDENTIAL AND TREASURY MANAGEMENT INDICATORS

- 8.1 During the six months to 30th September 2019, the Council operated within its prudential limits set out in the Prudential Code report approved by Council in March 2019. Details of limits and actual performance are as follows:

8.2 Capital Expenditure and the Capital Financing Requirement

8.2.1 The Capital Expenditure plans of the Council are primarily financed by capital receipts and capital grants. The remaining element which cannot be immediately financed from other resources will constitute our borrowing requirement. The estimated level of available capital resources is provided in summary as the Capital Expenditure Indicator below.

Indicator: Capital Expenditure

	2019/20 Original Estimate £M	2019/20 Projected Outturn £M	2020/21 Revised Estimate £M	2021/22 Revised Estimate £M
Supported spend	81.643	112.404	37.727	19.522
Unsupported spend	37.047	39.822	11.807	2.756
Total spend	118.690	152.226	49.534	22.278
Financed by:-				
Borrowing	43.953	46.728	18.713	9.662
Other Capital Resources (Grants, Capital Receipts)	74.737	105.498	30.821	12.616

8.2.2 The Capital Financing Requirement (CFR) represents the Council's underlying need to borrow for capital purposes. The CFR is capital expenditure that has not yet been paid for from either revenue or capital resources.

8.2.3 The Council's expectation for the CFR for the next three years is shown below.

Indicator: Capital Financing Requirement (CFR)

	2019/20 31/03/20 Original Estimate £M	31/03/20 Projected Outturn £M	2020/21 31/03/21 Revised Estimate £M	2021/22 31/03/22 Revised Estimate £M
CFR	505.600	503.721	508.704	504.042
Net movement in CFR			4.983	(4.662)

8.2.4 The expected external debt for each year is as detailed below.

Indicator: External Debt

	30/09/19 Actuals £M	2019/20 31/03/20 Original Estimate £M	2019/20 31/03/20 Revised Estimate £M	2020/21 31/03/21 Revised Estimate £M	2021/22 31/03/22 Revised Estimate £M
Borrowing	357.854	378.447	374.645	424.193	463.707
Other long term liabilities	0.457	0.584	0.584	0.583	0.583
Total External Debt	358.311	379.031	375.229	424.776	464.290

8.2.5 Other Long Term Liabilities represents the Council's obligation under its finance leases.

9.0 LIMITS TO BORROWING ACTIVITY

9.1 The first key control over the Council's activity is to ensure that, over the medium term, borrowing will only be for a capital purpose. The Council needs to ensure that external borrowing does not exceed the total of the capital financing requirement in the preceding year plus the estimate of the additional capital financing requirement for the next three financial years. This allows some flexibility within a three-year period to deliver an effective Treasury Management strategy.

Borrowing Activity (Gross Borrowing)

	30/09/19 Actuals £M	2019/20 31/03/20 Original Estimate £M	2019/20 31/03/20 Revised Estimate £M	2020/21 31/03/21 Revised Estimate £M	2021/22 31/03/22 Revised Estimate £M
Gross Borrowing (inc. Other Long Term Liabilities)	358.311	379.031	375.229	424.776	464.290
Capital Financing Requirement		505.600	503.721	508.704	504.042

9.2 The Authorised Limit represents the limit beyond which borrowing is prohibited, and needs to be set, monitored and revised by Members. It reflects the maximum level of borrowing to fund existing capital commitments, which could be afforded in the short term, but is not sustainable. It is the expected maximum borrowing need, with some added headroom for unexpected movements. It is proposed that these limits be

amended in line with increases to the underlying need to borrow, that is, the Capital Financing Requirement.

Indicator: The Authorised Limit

	2019/20 30/09/19 Actuals £M	2019/20 Limit £M	2020/21 Limit £M	2021/22 Limit £M
Gross Borrowing	357.854	510.000	510.000	510.000
Other long term liabilities	0.457	2.000	2.000	2.000
Authorised Limit	358.311	512.000	512.000	512.000

- 9.3 The Operational Boundary is based on the probable external debt during the course of the year; actual borrowing could vary around this boundary, for short times, during the year. It should act as an indicator to ensure the Authorised Limit is not breached.

Indicator: The Operational Boundary

	2019/20 30/09/19 Actuals £M	2019/20 Estimate £M	2020/21 Estimate £M	2021/22 Estimate £M
Gross Borrowing Limit	357.854	380.000	425.000	460.000
Other long term liabilities	0.457	1.000	1.000	1.000
Operational Boundary	358.311	381.000	426.000	461.000

10.0 AFFORDABILITY PRUDENTIAL INDICATORS

- 10.1 Previous sections have covered overall capital and control of borrowing indicators, but there is also a requirement to assess the affordability of capital investment plans. This provides an indication of the impact of the capital investment plans on the overall Council finances.
- 10.2 The Ratio of Financing Costs to Net Revenue Stream identifies the trend in the cost of capital (borrowing costs net of interest and investment income) against the "net revenue stream". The net revenue stream for the General Fund is the amount collectable from Council Tax payers added to the Council's Revenue Support Grant (RSG) and Non Domestic Rates (NDR). The key use of this indicator is to compare trends in the ratio of financing costs to the net revenue stream, over time.

Indicator: Ratio of Financing Costs to Net Revenue Stream

	2019/20 Original Estimate	2019/20 Revised Estimate	2020/21 Revised Estimate	2021/22 Revised Estimate
General Fund	4.86%	4.95%	5.38%	5.57%

- 10.3 A LOBO is a financial instrument called a “Lender’s Option Borrower’s Option”. It provides a lower rate of interest for the initial period and a higher rate for the rest of its term (reversionary period), albeit that the higher rate was comparable with interest rates prevailing at the time the loans were taken. At the end of the initial period and at six monthly intervals, the lender has the option to increase the interest rate payable. This provides the Council with the option to repay the loan if the terms are not acceptable. It is the view of our Treasury Management Advisors that it is unlikely the LOBO’s will be called within this financial year.
- 10.4 The revised amount of LOBO debt held in 2019/20 is £31m, 9%. Although not a requirement of the Prudential Code, an internal limit of LOBO debt is set as follows:

	£M	% of Debt Portfolio
LOBO Limits	50	20

- 10.5 The maturity structure indicator sets gross limits to reduce the Council’s exposure to large fixed rate sums falling due for refinancing annually. The Code of Practice requires LOBO’s to be represented in the maturity structure at the next option date, hence the table below demonstrates a high maturity within 12 months.

Indicator: Maturity Structure

	2019/20 Actuals as at 30/09/19	Upper Limit	Lower Limit
Under 12 months	13%	70%	0%
12 months to 2 years	3%	70%	0%
2 years to 5 years	10%	60%	0%
5 years to 10 years	17%	70%	0%
10 years to 20 years	8%	90%	0%
20 years to 30 years	0%	90%	0%
30 years to 40 years	49%	90%	0%
40 years to 50 years	0%	90%	0%

- 10.6 In order to maximise investment returns there could be opportunities for sums to be invested for longer than one year. This would only be undertaken with a prudent view of the primary considerations of security and liquidity.

11.0 NON SPECIFIED INVESTMENTS

- 11.1 The Investment Strategy enables lending to organisations upon which we undertake appropriate due diligence and put in place appropriate security arrangements. Such loans could result in the Council being able to achieve better investment returns at an acceptable level of risk and to secure base budget savings over the short to medium term to protect frontline services whilst supporting initiatives for purposes relevant to Council functions and priorities.
- 11.2 Investment decisions in these “Non Specified Investments” are subject to S151 officer determination, following appropriate due diligence and subject to appropriate and acceptable security arrangements being in place as part of the commercial agreement.
- 11.3 The maximum exposure for this type of investment is set at £25M with a maximum maturity limit of 30 years.
- 11.4 Such transactions will be included in the indicators reported as part of the quarterly performance reports and statutory Treasury Management Reports.

Indicator: Total principal funds invested for periods longer than 1 year:

	Limit	31/03/20 Estimate
Maximum principal sums invested over 1 year	£25m	£4.5m

- 11.5 The £4.5m represents the Council’s commercially agreed 10-year loan to Trivallis.
- 11.6 For measuring the Council’s exposure to interest rate risk, the following table shows the revenue impact of a 1% rise or fall in interest rates (based on borrowing and investments as at 30th September 2019):

Interest Rate Risk	Impact £M
One year revenue impact of a 1% rise/fall in interest rates	0.128

12.0 INVESTMENT STRATEGY, ACTIVITY & RESULTS

- 12.1 The Council manages its investments in-house, investing in line with the Council’s approved lender criteria as approved by Council on the 27th March 2019.

- 12.2 Members will recall that following the onset of the unprecedented national and international economic crisis in 2008, all of this Council's cash flows are currently being invested in the Debt Management Account Deposit Facility and other Government backed public sector bodies, in line with the aforementioned approved strategy. This strategy ensures we prioritise **Security** (protecting monies invested), then **Liquidity** (cashflow) and finally **Yield** (return on investment). The order of these "SLY" priorities are detailed in Investment Guidance produced by the Welsh Government.
- 12.3 I have kept this under constant review subsequently with a view to returning to market investment activity at an appropriate time. To date, the Council has not returned to market investments. Members will be kept informed of any changes as part of the Council's quarterly performance reports.
- 12.4 The following table shows the overall result of the investment activities undertaken by the Council:

	Interest Received £M	Average Cash Balance £M	Return on Investments %	Benchmark Return %
General Balances	0.96	16.91	0.57	0.53

The benchmark for Local Authority internally managed funds is the average 7-day LIBID rate.

13.0 TREASURY MANAGEMENT ADVISORS

- 13.1 The Council appointed Arlingclose as its Treasury Management Advisors during March 2019 and they continue to support the Council's Treasury Management function.

14.0 TRAINING

- 14.1 Officers have attended events hosted by Arlingclose which provide an overview of the economic environment, investment and borrowing, treasury management related accounting changes and associated implications for the Council. In addition, strategy meetings have been held between Arlingclose and officers in July and September this year. Officers continue to receive interest rate information, economic data, credit ratings and general market environment information on a regular basis.

15.0 MINIMUM REVENUE PROVISION (MRP)

- 15.1 In accordance with legislative requirements applicable to local government (Local Government Act 2003), there is a requirement to charge an amount to revenue each year in respect of capital expenditure that is funded by

borrowing. This charge is known as Minimum Revenue Provision (MRP) and must be a prudent amount in accordance with Welsh Government Statutory Guidance.

- 15.2 The method of charging MRP for Supported Borrowing is a straight line policy over 40 years. With regard to finance leases MRP is equivalent to the principal value of repayments. With regard to the method of charging MRP to Council Fund Balances in respect of Unsupported Borrowing only, the method used is dependent upon the type of asset being created as set out in the approved MRP Policy statement approved by Council on the 27th March 2019.

16.0 EQUALITY AND DIVERSITY IMPLICATIONS

- 16.1 The report provides an overview of the Council's Treasury Management activities during the first six months of 2019/20 in line with the Treasury Management and Capital Strategies approved by Council in March 2019. As a result, no Equality Impact Assessment is required for the purposes of this report.

17.0 CONSULTATION

- 17.1 Following consideration by Council, this report will be presented to the Finance and Performance Scrutiny Committee in line with the laid down code of practice "CIPFA Treasury management in the Public Services 2017" and also the Terms of Reference for this Committee.

18.0 FINANCIAL IMPLICATION(S)

- 18.1 The financial results / implications of the Council's Treasury Management arrangements during the first six months of 2019/20 have been incorporated into quarterly Performance Reports during the year.

19.0 LEGAL IMPLICATIONS OR LEGISLATION CONSIDERED

- 19.1 The report ensures the Council complies with its legal duty under the Local Government Act 2003 and in doing so is in line with the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities.

20.0 LINKS TO CORPORATE AND NATIONAL PRIORITIES AND THE WELL-BEING OF FUTURE GENERATIONS ACT

- 20.1 This report evidences the progress made in delivering the Council's Corporate Plan – *'The Way Ahead'* in particular through supporting the

'Living Within Our Means' theme by pursuing optimum treasury management performance or return at the same time as managing associated risk.

- 20.2 The report also supports the Well-being of Future Generations Act in particular 'a globally responsible Wales' through responsible management and investment of the Council's resources.

21.0 CONCLUSION

- 21.1 The 2019/20 financial year continues to be a challenging year for Treasury Management and this report highlights for Members the Treasury Management activities that have been undertaken between April and September 2019.

Appendix 1

TREASURY MANAGEMENT POLICY STATEMENT

Rhondda Cynon Taf County Borough Council defines the policies and objectives of its treasury management activities as:

- The management of the organisation's borrowing, 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.
- This Authority regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Authority, and any financial instruments entered into to manage these risks.
- This Authority acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

ADOPTION OF TREASURY MANAGEMENT CLAUSES

- This Authority will create and maintain, as the cornerstones for effective treasury management:
 - a Treasury Management Policy Statement, stating the policies, objectives and approach to risk management of its treasury management activities; and
 - suitable treasury management practices (TMPs), setting out the manner in which it will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.
- This Authority will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.
- This Authority delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Council, and

for the execution and administration of treasury management decisions to the Director of Finance and Digital Services, who will act in accordance with the organisation's policy statement and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

- This Authority nominates the Finance and Performance Scrutiny Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

Other information:

Relevant Scrutiny Committee – Finance and Performance Scrutiny Committee

LOCAL GOVERNMENT ACT 1972

AS AMENDED BY

THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) ACT 1985

RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL

COUNCIL 27TH NOVEMBER 2019

REPORT OF THE DIRECTOR OF FINANCE AND DIGITAL SERVICES

**Item: 2019/20 MID YEAR TREASURY MANAGEMENT STEWARDSHIP
REPORT**

Background Papers

- 27th March 2019 Council meeting – Reports:
 - Treasury Management Strategy Incorporating Investment Strategy, Treasury Management Indicators and MRP Statement for 2019/20.
 - 2019/20 Capital Strategy Report Incorporating Prudential Indicators.

These reports were also presented to the Finance and Performance Scrutiny Committee on 2nd April 2019.

Officer to contact: Barrie Davies (Director of Finance and Digital Services)
