



RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL

COUNCIL

25TH JULY 2018

20017 / 18 ANNUAL TREASURY MANAGEMENT REVIEW

REPORT OF THE GROUP DIRECTOR, CORPORATE AND FRONTLINE SERVICES

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1.0 PURPOSE OF REPORT

1.1 This report constitutes the statutory requirement to provide Members with information on :-

- the Council's Treasury Management activity during 2017/18; and
- the actual Prudential and Treasury Indicators for 2017/18.

2.0 RECOMMENDATIONS

2.1 It is recommended that Members note the content of the report.

3.0 INTRODUCTION

3.1 Treasury Management is defined as:

“The management of a local authority’s cash flows, its borrowings and its investments, the management of the associated risks, and the pursuit of the optimum performance or return consistent with those risks”.

3.2 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. The Council is required to comply with both Codes through Regulations issued under the Local Government Act 2003.

3.3 The primary requirements of the Codes are as follows:

- Creation and maintenance of a Treasury Management Policy;

- Creation and maintenance of Treasury Management Practices, which set out the manner in which the Council will seek to achieve stated policies and objectives;
- Approval by Council (by 31st March) of a Treasury Management Strategy Report (including Prudential and Treasury Indicators and an Investment Strategy) for the year ahead, an Annual Review Report of the previous year and a Mid Year Review; and
- Effective scrutiny of the Treasury Management function.

Rhondda Cynon Taf C.B.C. complies with these requirements and supplements this by including detail of our treasury activities and prudential indicators in the quarterly Council performance reports to Members.

3.4 During 2017/18, the Finance and Performance Scrutiny Committee has continued to scrutinise the Treasury Management function via quarterly performance reports and reviews of the strategy and mid year position.

3.5 This annual report will cover the following areas of treasury activity during 2017/18:

- Treasury Management advisors;
- Economic background;
- Borrowing strategy;
- Borrowing activity and results;
- Estimated and actual treasury position and prudential and treasury indicators;
- Investment strategy; and
- Investment activity and results.

3.6 It should be noted that the accounting practice to be followed by the Council requires financial instruments in the accounts (debt, investments, etc) to be measured in a method compliant with International Financial Reporting Standards. The figures in this report are based on the principal amounts borrowed and invested and so may differ from those in the Council's Statement of Accounts.

4.0 TREASURY MANAGEMENT ADVISORS

4.1 The Council appointed Arlingclose as its Treasury Management Advisors during March 2014. The contract was for an initial 3 year period, with the option taken to extend for a further 2 years up to 31st March 2019.

4.2 To date the service provided has been good. The Council will continue to monitor the advisor's performance. If any adverse performance or contractual issues arise, Members will be informed accordingly.

- 4.3 The Council recognises that although information and advice is provided via the contract, responsibility for Treasury Management decisions remains with the Council.

5.0 ECONOMIC BACKGROUND

5.1 General Economic Background

- 5.1.1 The UK economy still faces a challenging outlook as the minority government continues to negotiate the country's exit from the European Union. GDP grew by 1.8% in 2017, for 2018 the growth forecast is 1.5%, with the forecasts for 2019 and 2020 remaining unchanged at 1.3%.
- 5.1.2 The inflationary impact of rising import prices, a consequence of the fall in sterling following the outcome of the EU referendum, resulted in year-on-year CPI rising to 3.1% in November 2017 before falling back to 2.7% in February 2018 and 2.5% in March 2018.
- 5.1.3 The Bank of England's Monetary Policy Committee increased the Bank Rate by 0.25% to 0.5% on 1st November 2017, the first rise in ten years.
- 5.1.4 The labour market showed resilience as the unemployment rate fell back to 4.3% in January 2018. Real average wage growth turned negative before slowly recovering and is expected to be positive in 2018/19.
- 5.1.5 The Council continued to maintain a low risk strategy throughout the year to ensure exposure to any capital loss was minimised.

5.2 Short term investment rates

- 5.2.1 The Council's investment income is subject to changes in short term interest rates. The level of the Bank Rate is one of the main determinants of the rate of interest the Council receives on its short term investments. The forward looking estimate of the Bank Rate, as provided by our Treasury Management advisors, is for the rate to increase to 0.75% in 2018 and then increase twice in 2019 to 1.25%.

5.3 Longer term interest rates

- 5.3.1 The majority of the Council's borrowing is from the PWLB (Public Works Loan Board). Long-term borrowing rates are influenced by gilt yields which are driven by inflation and demand/supply considerations.
- 5.3.2 During August 2012, HM Treasury introduced "the certainty rate", whereby local authorities are able to access borrowing at 0.2% cheaper than published PWLB rates. In order to access the discounted rate, authorities were required to provide Welsh Government (and onward, the Debt

Management Office) with an indication of their potential borrowing requirements for the next 3 years.

5.3.3 In December 2017, the UK Government announced plans to make available an amount of lending at the Local Infrastructure Rate whereby local authorities are able to access borrowing at 0.4% cheaper than published PWLB rates. A corresponding share has been made available to local authorities in Wales and Welsh Government has allocated a set amount across all 22 Welsh authorities, this Council being allocated £4.4m. This rate will be available from June 2018 with a period of 3 years to draw down the allocation.

5.3.4 PWLB rates during 2017/18 were as follows (these are the “certainty rates”):

	5 years	10 years	20 years	50 years
Average	1.56%	2.13%	2.65%	2.41%
Highest	2.07%	2.57%	2.93%	2.72%
Lowest	1.00%	1.64%	2.27%	2.05%

6.0 BORROWING STRATEGY

6.1 The borrowing strategy for 2017/18 approved by Council in March 2017 stated that the borrowing requirement to fund the 2017/18 Capital Programme was £40.0m. In line with the capital programme, the borrowing requirement decreased to £35.6m during the year largely due to the re-profiling of the 21st Century Schools schemes. It was also reported that the cheapest form of borrowing would be “internal borrowing” by running down cash balances and foregoing interest earned at historically low rates. This also minimises counterparty risk (risk that an investment may become irrecoverable).

6.2 The strategy also reported that the Section 151 Officer, under delegated powers, would take the most appropriate form of borrowing depending upon the prevailing interest rates at the time, taking into account advice provided by our advisors and an assessment of risk.

6.3 Affordability and the cost of carry remain important influences on the Council’s borrowing strategy. As short term interest rates have remained, and are likely to remain lower than longer term rates, short term cashflow shortfalls have been met by utilising short term loans.

6.4 In the 2017/18 strategy approved by Council in March 2017 it was also reported that the Council may reschedule debt where there is an opportunity to generate savings. However, changes in PWLB rate calculations have reduced the attractiveness of early repayments associated with rescheduling.

7.0 **BORROWING ACTIVITY AND RESULTS**

7.1 A summary of the Council's borrowing activity (excluding Finance Leases) can be seen in the table below:

	Opening Balance 1st April 2017	Movement	Closing Balance 31st March 2018	Average Debt	Total Interest	Average Interest
	£M	£M	£M	£M	£M	%
PWLB	109.297	0	109.297	109.297	5.257	4.81
Banks LOBOS	31.000	0	31.000	31.000	1.395	4.50
Banks Fixed Term	56.500	(2.000)	54.500	55.508	2.818	5.08
Other	0.073	(0.073)	0	0	0	0.00
Local Authorities	35.000	41.000	76.000	45.479	0.239	0.53
Total	231.870	38.927	270.797	241.284	9.709	4.02

7.2 Short term loans were taken to meet day to day cashflow requirements at an average rate of 0.53% during the year. In accordance with our risk strategy as detailed in section 6 above, to minimise investment exposure and counterparty risk on cash balances held, no new long term borrowing was undertaken during 2017/18.

7.3 During the year there was no variance reported in the Council's Net Capital Charge Budget of £19.6m, despite the challenges faced with investment income and maintaining our low risk strategy.

7.4 There were no opportunities to further reduce the cost of our borrowing via rescheduling during the year.

7.5 Members will also recall the previously reported position with regard to the accounting arrangements and treatment of LOBOs (Lender Option / Borrower Option). These loan instruments have enabled the Council to realise significant short-term and further ongoing reductions in its capital charges. These savings have been invested into key service improvements and the Treasury Management Reserve, which have helped not only to reduce risk around future financial market changes, but also as pump priming to produce more efficient and effective on-going front line services for the taxpayer.

8.0 ESTIMATED AND ACTUAL TREASURY POSITION AND PRUDENTIAL AND TREASURY INDICATORS

8.1 During the financial year 2017/18, the Council operated within its limits set out in the Prudential Code report approved in March 2017. Details of limits and actual performance are as follows:

		2017/18 Actual £
Capital Expenditure 17/18		101.761M
Capital Financing Requirement (CFR) as at 31 st March 2018		435.595M

Limit / Indicator	2017/18 Limit / Indicator	2017/18 Actual
Authorised Limit (£) (Limit beyond which borrowing is prohibited)	460.000M	275.229M (at highest point in year)
Operational Boundary (£) (Indicator to ensure Authorised Limit not breached)	321.000M	271.320M (at year end)
External Debt (£)	314.725M	270.797M
Other Long Term Liabilities	<u>0.450M</u>	<u>0.137M</u>
Sub total	315.175M	270.934M
Other : Finance Lease	<u>0.386M</u>	<u>0.386M</u>
Borrowing + Other Long Term Liabilities	315.561M	271.320M
Ratio of Financing Costs to Net Revenue Stream	4.84%	4.34%
Limit on Fixed Interest Rates	45% - 125%	77%
Limit on Variable Interest Rates	-25% - 55%	23%
Funds invested for greater than 1 year (£)	25M	5M
	£50M / 20% of debt	£31M / 11% of debt

LOBO Limit	portfolio	portfolio
Maturity Structure of Fixed Rate Debt	Under 12 mths 0-70%	Under 12 mths 16%
	12 mths – 2 yrs 0-70%	12 mths – 2 yrs 0%
	2-5 years 0-60%	2-5 years 0%
	5-10 years 0-70%	5-10 years 1%
	10-20 years 0-90%	10-20 years 0%
	20-30 years 0-90%	20-30 years 0%
	30-40 years 0-90%	30-40 years 80%
40-50 years 0-90%	40-50 years 3%	

9.0 **INVESTMENT STRATEGY**

- 9.1 The Council manages its investments in-house, investing during 2017/18 in line with the Council's approved lender criteria as approved by Council on the 15th March 2017. Investment policy is governed by Welsh Government guidance.
- 9.2 The Council's temporary cash flows are currently being invested in the Debt Management Account Deposit Facility and other Government backed public sector bodies. The Council supplements this strategy with lending to organisations subject to S151 officer determination, following appropriate due diligence and subject to appropriate and acceptable security arrangements. This low risk strategy was formed balancing risk and return. It is acknowledged that low risk investment strategies result in lower investment returns.
- 9.3 A number of AAA rated money market funds have been set up to provide further diversification options if the opportunity arises in the future. These accounts have not been used during 2017/18. Members will be kept informed of any changes as part of the Council's quarterly performance reports.
- 9.4 During the year, the Council has complied with the approved strategy and there have been no liquidity difficulties.
- 9.5 On the 29th November 2017, as part of the 2017/18 Mid Year Treasury Management Stewardship Report, Council approved the provision of Bridge Loan finance to CSC Foundry Ltd. CSC Foundry Ltd has been established by the 10 Councils of the Cardiff Capital Region City Deal in order to implement and contract with IQE Silicon Compounds Ltd to deliver the CSC project. CSC Foundry is a company limited by shares equally held by the 10 Councils.
- 9.6 A loan was provided for £1.7m (on the 14th March 2018) which was subsequently repaid to the Council on 29th March, following the agreement of the Joint Working Agreement (JWA) Business Plan by all 10 Councils.

10.0 INVESTMENT ACTIVITY AND RESULTS

10.1 The following table shows the overall result of the investment activities undertaken by the Council:

	Interest Received	Average Cash Balance	Return on Investments	Benchmark Return
	£M	£M	%	%
Cash Balances	0.036	14.692	0.24	0.21

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

10.2 The Economic Background section of this report set out the continuing difficulties in economic conditions during this period. As a result of these conditions and our low risk strategy, interest rates on investments remain low, although higher than the benchmark rate.

11.0 EQUALITY AND DIVERSITY IMPLICATIONS

11.1 The report provides an overview of the Council's Treasury Management activities during 2017/18 in line with the Strategy approved by Council in March 2017. As a result, no Equality Impact Assessment is required for the purposes of this report.

12.0 CONSULTATION

12.1 Following consideration by Council, this report will be presented to the Finance and Performance Scrutiny Committee in line with the laid down codes of practice and also the Terms of Reference for this Committee.

13.0 FINANCIAL IMPLICATION(S)

13.1 The financial results / implications of the Council's Treasury Management arrangements in 2017/18 have been incorporated into quarterly Performance Reports during the year and also reported to Council on 29th November 2017 as part of the 2017/18 Mid Year Treasury Management Stewardship Report.

14.0 LEGAL IMPLICATIONS OR LEGISLATION CONSIDERED

14.1 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.

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

- 15.1 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.
- 15.2 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.

16.0 CONCLUSION

- 16.1 The last financial year has continued to be challenging in relation to Treasury Management and this report highlights for Members that all related activities have operated effectively and within budgetary and prudential limits.

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

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COUNCIL 25TH JULY 2018

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SERVICES**

Item: 2017/18 ANNUAL TREASURY MANAGEMENT REVIEW

Background Papers

- 15th March 2017 Council meeting – Report: Treasury Management Strategy Incorporating Investment Strategy, Prudential Indicators and MRP Statement for 2017/18. This report was also reported to the Finance and Performance Scrutiny Committee on 4th April 2017.
- 29th November 2017 Council meeting – Report: 2017/18 Mid Year Treasury Management Stewardship Report. This report was also reported to the Finance and Performance Scrutiny Committee on 29th January 2018.

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