2019/20 TREASURY MANAGEMENT MID-YEAR REVIEW

1 SUMMARY

1.1 The purpose of the report is to provide an update of the Council's Treasury Management activity for the period 1 April 2019 to 30 September 2019 in accordance with the Council's Treasury Management Policy and good practice in treasury management.

1.2 It is recommended that Review Committee notes the Council's treasury activities for the period ending 30 September 2019 and provides comments on the information presented in this report, before it is presented for approval by Full Council on 17 December 2019.

2 INTRODUCTION

2.1 The Council has adopted the Code of Practice on Treasury Management and a requirement of this is to produce a mid year review looking at the Authority's performance in line with the Treasury Management and Capital Strategy considered by this Committee on 5 February 2019.

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

2.3 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 liabilities.

2.4 Accordingly, 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*."

2.5 This mid-year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the 2019/20 financial year to 30 September 2019 (provided by the Council's treasury advisors);
- A review of the Treasury Management & Capital 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 compliance with Treasury and Prudential Limits for 2019/20.

2.6 The Council employs treasury advisors, Link Asset Services Ltd. to provide advice on its treasury management strategy and analysis of the economy and expectations for interest rates.

3 ECONOMIC UPDATE

3.1 2019 has been a turbulent year politically, with Boris Johnson replacing Teresa May as Prime Minister in June with a commitment to leave the EU on 31 October 2019. Subsequently the Government and EU agreed an extension to the leaving date of 31 January 2020. With a general election now scheduled for 12 December there remains much uncertainty as to the political outlook. The detail of any trade deal will need to be negotiated by the end of the current transition period in December 2020 unless a further extension is negotiated, or otherwise face a no deal exit on that date.

3.2 The Bank of England revised its inflation forecasts down to 1.25% in 2019, 1.5% in 2020, and 2.0% in 2021; hence the Monetary Policy Committee (MPC) views inflation as causing little concern in the near future.

3.3 If economic growth were to weaken considerably, the MPC has relatively little room for manoeuvre with Bank Rate still held at 0.75%. The Chancellor may choose to support growth by way of a fiscal boost by, for example, tax cuts, increases in the annual expenditure budgets of government departments and services and expenditure on infrastructure projects, in order to try to boost the economy. The Government has already made moves in this direction and both of the largest parties have made significant promises in their election manifestos to increase government spending. The Chancellor has also amended the fiscal rules in November to allow for an increase in government expenditure.

3.4 With regard to inflation, the Consumer Price Index has remained close to the Bank of England's target of 2% during 2019 but fell in October to 1.5%. It is likely to remain close to or under 2% over the next two years and so does not pose any immediate concern to the MPC at the current time. However, if there was a no deal Brexit, inflation could potentially rise towards 4%, primarily because of imported inflation on the back of a weakening pound.

3.5 With regard to the labour market, growth in overall numbers employed has been fairly resilient. The unemployment rate fell back to a 44 year low of 3.8% on the Independent Labour Organisation measure in September, despite the fall in numbers employed, due to numbers leaving the work force. Wage inflation has been reducing slightly as supply pressures in the labour market ease, with earnings growing by about 1.9% in real terms. As the UK economy is primarily services sector driven, an increase in household spending power is likely to support the overall rate of economic growth in the coming months.

3.6 The General Election could result in a potential loosening of monetary policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up although, conversely, a weak international backdrop could provide further support for low yielding government bonds and gilts.

3.7 The latest Link Asset Service's forecast of Bank of England Base Rate and PWLB rates is shown in the table below. They are based on an assumption that there is an agreed deal on Brexit, including agreement on the terms of trade between the UK and EU, at some point in time. Given the current level of uncertainties around the result of the general election due on 12 December and then subsequent developments, this is a major assumption and so forecasts may need to be materially reassessed in the light of events over the coming weeks or months.

3.8 If there were an eventual Brexit with no agreement on the terms of trade between the UK and EU, then it is likely that there will be a cut or cuts in Bank Rate to help support economic growth.

Link Asset Services Interest Rate View	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
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	1.25	1.25	1.25
3 Month LIBID	0.70	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.30	1.30
6 Month LIBID	0.80	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40	1.50	1.50	1.50	1.50
12 Month LIBID	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60	1.70	1.70	1.70	1.70
5yr PWLB Rate	2.30	2.40	2.40	2.50	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.10	3.20	3.20
10yr PWLB Rate	2.60	2.70	2.70	2.70	2.80	2.90	3.00	3.10	3.20	3.20	3.30	3.30	3.40	3.50
25yr PWLB Rate	3.20	3.30	3.40	3.40	3.50	3.60	3.70	3.70	3.80	3.90	4.00	4.00	4.10	4.10
50yr PWLB Rate	3.10	3.20	3.30	3.30	3.40	3.50	3.60	3.60	3.70	3.80	3.90	3.90	4.00	4.00

4 KEY MOVEMENT/CHANGES TO THE CAPITAL AND TREASURY STRATEGIES

4.1 The Treasury Management & Capital Strategy Statement (TMCSS) for 2019/20 was approved by Full Council on 12 February 2019 as part of the Medium Term Financial Strategy.

4.2 There are no policy changes to the TMCSS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

5 PRUDENTIAL INDICATOR FOR CAPITAL INVESTMENT

5.1 This table shows the forecasted outturn for capital expenditure as at 30 September 2019 and the changes since the Capital Programme was agreed on 12 February 2019, as well as the indicative financing for the programme.

The main changes include £1.37m of expenditure relating to capital programme underspends carried forward from 2018-19, and £0.19m expenditure for electric charging points funded by grant.

Capital Expenditure	**2019/20 Original Estimate £'000s**	**2019/20 End of Year Forecast £'000s**
Total	**1,790**	**3,350**
Financed by:		
Revenue Contribution	255	255
S106 income	25	25
Disabled Facilities Grant via Better Care Fund	500	717
Capital Finance Reserve	252	819
New Homes Bonus	658	658
Air Quality Grant Income	0	602
IT Reserve	0	148
Transformation Reserve	100	126
Total Financing	**1,790**	**3,350**

Changes to the Prudential Indicators for the Capital Financing requirement and the Operational Boundary

5.2 Net external borrowing should not, except in the short term, exceed the total of Capital Financing Requirement (CFR) in the preceding year plus the estimates of any additional CFR for 2019/20 and next two financial years. The Council currently has no external borrowing, with the residual CFR relating to historic capital programme financing.

£000s	**2018/19 Actual**	**2019/20 Estimate**	**2020/21 Estimate**	**2021/22 Estimate**
CFR	777	777	777	777
Movement in CFR	-	-	-*	-*

* No movement is projected in the current estimates, but this will be subject to review ahead of the 2020/21 Treasury Management and Capital Strategy being presented to Review Committee in February 2020.

5.3 The 2008 Capital Finance and Accounting Regulations include a requirement to make prudent annual provision for repayment of debt arising from capital expenditure (known as a Minimum Revenue Provision or MRP). This is to ensure that debt is repaid over a period commensurate with that over which the capital expenditure provides benefits. If the Council does decide to borrow externally in future an MRP policy will need to be agreed and implemented. This would be set out in the relevant Treasury Management Strategy Statement for the year.

5.4 There are no changes to the Authorised and Operational limits for 2019/20 (upper limit beyond which external debt is prohibited) which are agreed in the Treasury Management Strategy and can only be revised by Full Council. As there has been no borrowing, there has not been any breach of these limits.

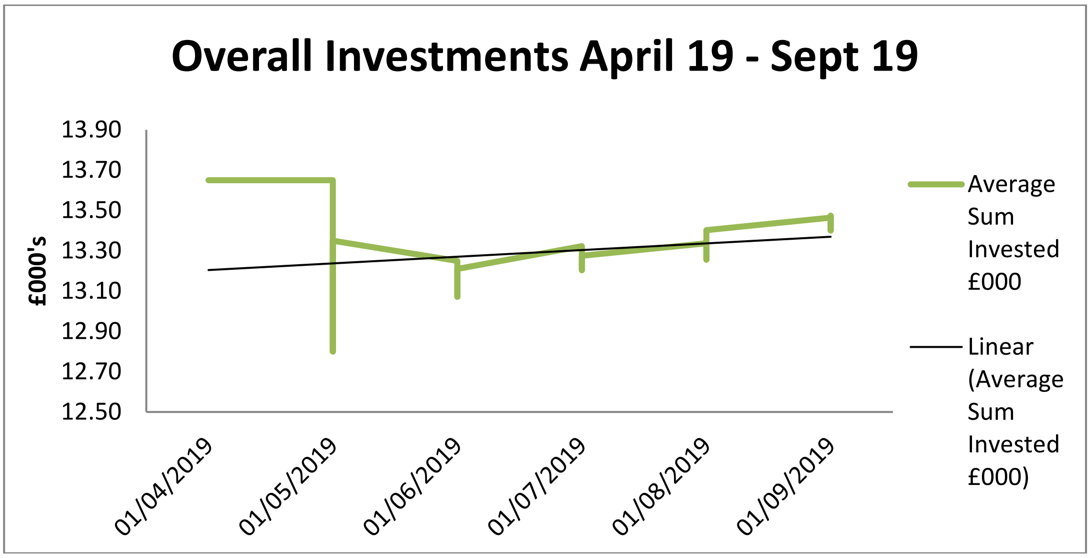
6 INVESTMENT PORTFOLIO 2019/20

6.1 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. Given this risk environment, investment returns are likely to remain low.

6.2 The Council started the year with £12.150m of investments and £1.804m in its main current account. The balance of investments held as at 30 September 2019 was £13.050m, plus £0.706m in the main current account. The table below summarises the investment transactions that have taken place.

	Investments £000's	Current Account £000's	No. of Investments
Balance on Investments 1 April 2019	12,150	1,804	6
Investments placed 01/04/19 – 30/09/19	27,850		
Investments realised 01/04/19 – 30/09/19	26,950		
Balance on Investments 30 Sept 2019	13,050	706	5

6.3 The graph below shows the average investments held by the authority. The reductions in the average balances relate to the regular payments to precepting bodies, which are then replenished at the start of the following month through Direct Debits for Council Tax and Business Rates.



6.4 The five investments comprising the balance of £13.050m were placed with the following counterparties:

Counterparty	Investments £000's	Investments %
Santander 95 day account	3,650	28
Lloyds 95 day account	3,000	23
Lloyds 365 day account	1,000	8
Money Market Prime	4,200	32
Money Market Deutsche	1,200	9

6.5 Forecast investment return for 2019/20 is £130,000 compared to a budget of £80,000, partly due to the average length of investment increasing slightly (with a commensurate increase in returns) and the Council seeking out the best returns within its agreed parameters and risk appetite as set out in its Treasury Management Strategy. The investment rates on offer for short term deposits have remained in line with Bank of England base rate, whilst longer term investment provides a slightly higher rate. The table below shows the returns the Council are receiving compared to financial benchmarks.

Investment performance for year to date at 30 September 2019

Benchmark	Benchmark Return (%)	Council Performance (%)	Investment Interest Earned (£)
7 day	0.57	0.75	246
1 month	0.60	0.79	3,997
3 month	0.66	1.05	3,797
6 month	0.73	1.02	39,507
12 month	0.83	1.25	12,226
Total			**59,773**

6.6 The Section 151 Officer confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2019/20. A review of the Council's investment strategy will be undertaken in the New Year and reported in the 2020/21 Treasury Management & Capital Strategy.

Investment Counterparty criteria

6.7 The current investment counterparty criteria selection approved in the TMS is meeting the requirement of the treasury management function.

6.8 The financial institutions with which the Authority is investing are monitored on a regular basis in line with the risk document issued by Link, the treasury advisors.

7 RISK IMPLICATIONS

7.1 There are no new risk management implications arising from the contents of this report. However, Members will be aware of the uncertainty in the financial markets and the economy as a whole and the potential risks that this may have in general. The Council's TMS outlines the risks involved in the investments made by the Council and there have been no changes to the assessment of risk.

8 EQUALITY & DIVERSITY IMPLICATIONS

8.1 An Equality Impact Assessment has not been completed as no decision is being made.

9 RECOMMENDATION

It is proposed that the Review Committee **RESOLVES** to recommend the contents of this Treasury Management Mid Year Report to Full Council.

Naomi Lucas
Section 151 Officer

Background Papers:- None.

For further information please contact Carrie Cox on:-
Phone: 01702 318029
Email: carrie.cox@rochford.gov.uk

If you would like this report in large print, Braille or another language please contact 01702 318111.