ANNEX C

TREASURY MANAGEMENT POSITION 2018/19 – QUARTER 1

1.0 LEGISLATIVE REQUIREMENT:

1.1 The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management recommends that members be updated on treasury management activities regularly (Treasury Management Strategy Statement, Annual and Mid-year reports, as well as quarterly updates). This report therefore ensures this Council is implementing best practice in accordance with the Code.

1.2 The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This Quarter 1 report therefore updates Members on the current treasury management position and is presented to Cabinet and also Audit, Governance and Standards Committee.

1.3 The Council's treasury management position is based on its requirement to fund the capital programme and it's operational cash flow need. The Council looks to balance the requirement to borrow from external sources with the surplus funds that are available.

1.4 During 2017/18 the Council supported its Capital Expenditure by capital receipts, reserves, revenue contribution, long term borrowing , as well as short term borrowing and the use of surplus funds for cash flow purposes. The short term borrowing was taken and repaid in Quarter 1 of 2018/19. The council continues to have an underlying need to borrow for capital purposes and has long term external borrowing of £1,200,000 which was undertaken in September 2016 from the Public Works Loan Board (PWLB) at a rate of 1.05% over 5 years.

1.5 The capital financing requirement in 2018/19, which is the amount of borrowing required to support the capital expenditure programme, is set at £36,200,000. The capital expenditure of the Council is mainly supported by grants, contributions and reserves. The capital financing requirement refers to the amount of borrowing that could be taken to support the capital expenditure programme.

1.6 The following table shows the treasury management position as at 30 June 2018:-

	30 June 18 £000's	Rate %
Capital Financing Requirement	36,200	
Borrowing	1,200	1.05
Investments	780	0.43

Table 1: Borrowing and Investment position at 30 June 2018

1.7 The table shows that changes in the capital expenditure programme only affects the treasury management position through the surplus funds that are available to the Council to invest, to earn investment income.

1.8 In December 2017, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued a revised Treasury Management Code and Cross Sectoral Guidance Notes, and a revised Prudential Code. A particular focus of these revised codes was how to deal with local authority investments which are not treasury type investments e.g. by investing in purchasing property in order to generate income for the Authority at a much higher level than can be attained by treasury investments. The Council will provide a report on the overall capital strategy and show how the new cash resources of the Authority are apportioned between treasury and non-treasury investments. Officers will report to members at Quarter 2 when the implications of these new codes have been assessed as to the likely impact on this Authority

2.0 THE ECONOMY, INTEREST RATES AND TREASURY MANAGEMENT STRATEGY:

2.1 The economic background and interest rate forecast, which sets the environment in which the Council's treasury management operates, is attached at Annex D.

3.0 ANNUAL INVESTMENT STRATEGY 2018/19 – QUARTER 1:

3.1 The Treasury Management Strategy Statement (TMSS) for 2018/19 which includes the Annual Investments Strategy, was approved by the Council on 27 February 2018. It sets out the Council's investment priorities as being:

- Security of capital;
- Liquidity;
- Yield

3.2 The Council's priority is security of its surplus funds when investing with financial institutions. However the Council will always aim to achieve the optimum return (yield) on investments in line with its risk appetite and which is commensurate with proper levels of liquidity and security. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months. Investments are placed with highly credit rated financial institutions, using the Council's treasury Management advisers – Link Asset Services - suggested creditworthiness approach including sovereign credit rating and Credit Default Swap (CDS) overlay information provided by Link Asset Services.

3.3 The average level of funds available for investment purposes during Quarter 1 – 30 June 2018 - was £5,990,000. The level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme. The Council held £780,000 cash flow movement balances at the end of Quarter 1.

3.4

Benchmark	Benchmark Return	Council Performance	Investment Interest Earned
7 day	0.36%	0.43%	£6,451

Table 2: Investment performance for quarter 1 at 30 June 2018

3.5 The table shows that the Council monitors its cash flow investments against the 7 day rate. The Council outperformed the 7 day benchmark by 0.07%.

3.6 The Council's budgeted investment return for 2018/19 was approved at £8,000 and performance for the year to date is above the budget. In Quarter 1 monitoring it has been reported that due to the increase in the Base Rate from when the Original Budget was set, the investment rates available to the council has also increased, resulting in an estimated £15,000 additional income making the budget £23,000. This will be closely monitored throughout the year.

4.0 BORROWING 2017/18 – QUARTER 1

4.1 The Council had short term borrowing of £5,000,000 and long term borrowing of £1,200,000 at the beginning of 2018/19. The short term borrowing was repaid in the first quarter of 2018/19. The long term loan with the Public Works Loan Board (PWLB) is due to be repaid in September 2021.

4.2 Public Works Loan Board (PWLB) rates have not been on any consistent trend in this quarter. During Quarter 1, the 50 year Public Works Loan Board target (certainty) rate for new long term borrowing was marginally reduced to 2.40%. the council set is overall borrowing target arte at 3.10% at the beginning of the financial year, to cover all rates periods from 0 to 50 years.

4.3 The table below shows the Public Works Loans Board interest rates which were available for loans during Quarter 1 of 2018/19. The Public Works Loans Board is the mechanism by which the Government allows local authorities to borrow at slightly lower interest rates than are available to other institutions. Certainty rates, as detailed in the table, are interest rates available to local authorities if they inform the Government of their borrowing requirements at the beginning of the financial year and are 0.02% (or 20 basis points) below Public Works Loans Board rates. This was introduced by the Government in October 2012.

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.28%	1.67%	2.10%	2.52%	2.25%
Date	01/06/2018	29/05/2018	29/05/2018	29/05/2018	29/05/2018
High	1.57%	1.98%	2.43%	2.79%	2.53%
Date	17/04/2018	25/04/2018	25/04/2018	25/04/2018	25/04/2018
Average	1.44%	1.86%	2.29%	2.66%	2.40%

Table 3: Public Works Loan Board (PWLB) certainty rates, quarter ended 30 June 2018

4.4 **Treasury Borrowing**: Due to the overall financial position and the underlying need to borrow for capital purposes, external borrowing of £1,200,000 was undertaken in September 2016 from the Public Works Loan Board at a rate of 1.05% over 5 years.

4.5 The Council took a short term loan during Quarter 1 from a Local Authority on 24 May 2018 at a rate of 0.70% for cash flow purposes. This was repaid on 1 June 2018.

4.6 It is anticipated that more borrowing will be required during the financial year 2018/19 to support the overall Capital Programme and for cash flow purposes. It is estimated that £5,000,000 will be borrowed from the PWLB in the next six months.

4.7 **Rescheduling of Borrowing**: the Council did not reschedule the long term loan of £1,200,000.

4.8 **Repayment of Borrowing**: the Council repaid a short term loan from 2017/18 of £5,000,000 in Quarter 1 of 2018/19.

5.0 <u>COMPLIANCE WITH PRUDENTIAL AND TREASURY INDICATORS</u>:

5.1 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators (affordability limits) were approved in the Treasury Management Strategy Statement by Council on 27 February 2018 and are in compliance with the Council's Treasury Management Practices.

5.2 During the financial year to date the Council has operated within the Treasury and Prudential Indicators approved which are attached at Annex E.

5.3 Officers can confirm that the approved limits within the Annual Investment Strategy were not breached during the Quarter ended 30 June 2018.

ANNEX D

Economic Update

1.1 ECONOMIC BACKGROUND:

United Kingdom - Growth in 2017 was disappointingly weak in the first half of the year but picked up to 0.5% in quarter 3 and 0.4% in quarter 4. Growth in quarter 1 of 2018 was again disappointing, although on the first revision the rate improved from 0.1 to 0.2% to allay fears that the economy may have started a prolonged period of very weak growth. Initial indications in quarter 2 are that growth may have picked up speed to around 0.4%.

The main reason for weak growth during 2017 and 2018 has been that inflation has been exceeding pay growth until recently, meaning that there has been negative growth in consumer disposable income when consumer expenditure is the biggest driver of the services sector which accounts for about 75% of Gross Domestic Product.

The manufacturing sector was the bright spot in the economy in 2017 in terms of strong growth but Quarter 1 was the weakest quarter for one and a half years and forward indicators do not suggest a return to strong growth is likely.

During January and February financial markets were viewing a Bank Rate increase at the May Monetary Policy Committee (MPC) meeting as likely to be a near certainty after strong growth in the second half of 2017. However, the ensuing weeks before the meeting saw opinion turn right around and the Monetary Policy Committee did not disappoint by leaving rates unchanged due to concerns as to whether the weak growth in quarter 1 was indicative of the start of a prolonged slow down or just a temporary blip, to which bad weather had been just one contributor. Since May, opinion has again turned to suggest that an August Bank Rate increase is back on the cards.

However, there remains much uncertainty around the Brexit negotiations, consumer spending levels and business investment, so it is still far too early to be confident about how strong growth and inflationary pressures will be over the next two years, and therefore the pace of any rate increases.

European Union - A recovery to strong growth in 2016 and 2017 looks as if it will weaken somewhat going forward. Despite providing massive monetary stimulus, the European Central Bank has been struggling to get inflation up to its 2% target. However, in April the headline Eurozone rate jumped up from 1.4% to 1.9% although the core inflation rate was still subdued in rising from 0.7% to 1.1%. At its June meeting, the European Central Bank announced it would halve its monthly quantitative easing purchases from €30bn to €15bn, and then end all purchases after December. It is unlikely to make a start on increasing interest rates until late in 2019.

USA - Growth in the American economy was volatile in 2015, 2016 and 2017 during each year, with quarter 1 being particularly weak. The annual rate of Gross Domestic Product growth for 2017 was 2.3%. Quarter 1 in 2018 came in at 2.0%, down from 2.9% in the previous quarter. The Trump $1.5 trillion income tax cut package coming into effect in January 2018, is likely to boost growth to the Trump administration's 3% target. However, it is also likely to boost inflation at a time when spare capacity in the economy is minimal and unemployment, in particular, has fallen to the lowest level for 17 years, reaching 3.8% in May. The Fed has started on an upswing in rates with seven increases since the first one in December 2015, the latest one being in June 2018 to lift the central rate to 1.75 – 2.00%. There could be a further two or more increases in 2018. In October 2017, the Fed became the first major western central bank to make a start on unwinding quantitative easing by phasing in a gradual reduction in respect of reinvesting maturing debt.

Chinese economic growth - has been weakening over successive years, despite repeated rounds of central bank stimulus and medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems.

Japan.- The best economic run, (of positive growth for eight quarters), since the 1980s came to an end in quarter 1 with a contraction of -0.6% blamed on weak exports. However, it is still struggling to get inflation up to its target rate of 2% despite huge monetary and fiscal stimulus, with inflation falling to only 0.4% in May. It is also making little progress on fundamental reform of the economy.

1.2 INTEREST RATE FORECAST:

The Council's treasury advisor, Link Asset Services, has provided the following forecast:

	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Bank Rate	0.50%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.50%	1.50%
5yr PWLB Rate	2.00%	2.00%	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.40%	2.50%	2.50%
10yr PWLB View	2.40%	2.50%	2.60%	2.60%	2.70%	2.80%	2.80%	2.90%	2.90%	3.00%	3.00%
25yr PWLB View	2.80%	2.90%	3.00%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%	3.50%	3.50%
50yr PWLB Rate	2.50%	2.60%	2.70%	2.80%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%

Link Asset Services undertook its last review of interest rate forecasts on 11 May after the quarterly Bank of England Inflation Report and Monetary Policy Committee meeting at which the Monetary Policy Committee kept Bank Rate unchanged at 0.50%. The Monetary Policy Committee minutes indicated they wanted to see whether the slowdown in growth in quarter 1 had been a temporary blip or a potential first sign of a prolonged period of weak growth.

The overall balance of risks to economic recovery in the United Kingdom is probably even. However, given the uncertainties around Brexit in particular, but also other uncertainties, there is a wide diversity of possible outcomes for the strength of economic growth and inflation, and the corresponding speed with which Bank Rate could go up.

PRUDENTIAL AND TREASURY MANAGEMENT INDICATORS

It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits – the Authorised Limit and the Operational Boundary - as detailed below. The Council approved the Treasury and Prudential Indicators (affordability limits), for the 2018/19 financial year at Council on 26 February 2018 in the Treasury Management Strategy Statement.

The main purpose of the indicators is to control how much a Council needs to borrow.
In 2018/19, The Treasury Management Strategy Statement approved the capital financing requirement at £36.2 million which gives the Council the ability to either use surplus funds to support the capital expenditure for the loan to a local Housing Association or to take external borrowing.

The Prudential and Treasury Indicators are detailed below as approved at Council prior to the beginning of the 2018/19 financial year – Original Budget - and at Q1 Actual:

1. PRUDENTIAL INDICATORS	**2018/19**	**2018/19**
Extract from budget and rent setting report	**Original Budget**	**Actual Q1**
	£'000	**£'000**
Capital Expenditure	13,865	14,607
Ratio of financing costs to net revenue stream	Nil	Nil
Net borrowing requirement General Fund		
brought forward 1 April	11,900	1,200
carried forward 31 March	22,000	1,200
in year borrowing requirement	10,100	0
Capital Financing Requirement 31 March 2019	36,200	36,200
Incremental impact of capital investment decisions	£	£
Increase in Council Tax (band D) per annum	Nil	Nil

2. TREASURY MANAGEMENT INDICATORS	**2018/19**	**2018/19**
	Original Budget	**Actual Q1**
	£'000	**£'000**
Authorised Limit for external debt -		
borrowing	£40,000	£40,000
other long term liabilities	£1,000	£1,00
TOTAL	£41,000	£41,000
Operational Boundary for external debt -		
borrowing	£39,000	£39,000
other long term liabilities	£600	£600
TOTAL	£39,600	£39,600
Actual external debt	£22,000	£1,200
Upper Limit on fixed interest rates based on net debt	104%	104%

Upper Limit on variable interest rates based on net debt	-4%	-4%
Upper limit for total principal sums invested for over 364 days (per maturity date)	£1,000	£1,000

Maturity structure of fixed rate borrowing during 2018/19	Lower limit	Upper limit
Under 12 months	**0%**	**100%**
12 months to 2 years	**0%**	**100%**
2 years to 5 years	**0%**	**100%**
5 years to 10 years	**0%**	**100%**
10 years to 20 years	**0%**	**100%**
20 years to 30 years	**0%**	**100%**
30 years to 40 years	**0%**	**100%**
40 years to 50 years	**0%**	**100%**