Report Reference Number: E/19/02

To:	**Executive**
Date:	**30 May 2019**
Status:	**Non Key Decision**
Ward(s) Affected:	**All**
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Lead Executive Member:	**Councillor Cliff Lunn, Lead Executive Member for Finance and Resources**
Lead Officer:	**Karen Iveson, Chief Finance Officer**

Title: **Treasury Management – Annual Review 2018/19**

Summary:

This report reviews the Council's borrowing and investment activity (Treasury Management) for the period 1st April 2018 to 31st March 2019 (Q4) and presents performance against the Prudential Indicators.

Investments – On average the Council's treasury deposits totalled £63.413m over the year at an average rate of 0.81% earning interest of £518k (£356k allocated to the General Fund; £163k allocated to the HRA) which is £279k above budget. In line with the approved Medium Term Financial Strategy, general fund income above £300k should be transferred to Contingency reserve, resulting in year-end transfer of £56k.

Property Funds – A budget of £5m was approved to invest in Property Funds, split equally between Blackrock and Threadneedle. As previously reported entry fees of £76k were treated as revenue expenses and offset against returns in year one, resulting in net income of £6k and a closing investment value of £4.93m, a loss of 0.69% (£34.2k) against the original investment Excluding entry fees, the funds achieved a combined return revenue return of 4.13%

Loans to SDHT – During 2018/19 interest earned on loans to SDHT was £18k, in relation to Kirkgate and St Joseph's street Tadcaster.

Borrowing – Long-term borrowing totalled £59.3m at 31st March 2019, (£1.6m relating to the General Fund; £57.7m relating to the HRA),

Interest payments of £2.49m were made during 2018/19, a saving of £0.37m against budget, which is due to deferral of borrowing assumed for the Housing Development Programme. The Council had no short term borrowing in place as at 31 March 2018, and has not undertaken any during 2018/19.

Prudential Indicators – the Council's affordable limits for borrowing were not breached during this period.

Recommendations:

i. Councillors endorse the actions of officers on the Council's treasury activities for 2018/19 and approve the report.

ii. Note that investment income allocated to the General Fund, over the £300k threshold is to be transferred to Contingency Reserve – equating to £56k for the year.

Reasons for recommendation

To comply with the Treasury Management Code of Practice, the Executive is required to receive and review regular treasury management monitoring reports.

1. Introduction and background

1.1 This is the final monitoring report for treasury management in 2018/19 and covers the period 1 April 2018 to 31 March 2019. During this period the Council complied with its legislative and regulatory requirements.

1.2 Treasury management in Local Government is governed by the CIPFA "Code of Practice on Treasury Management in the Public Services" and in this context is the management of the Council's cash flows, its banking and its capital market transactions, the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks. This Council has adopted the Code and complies with its requirements.

1.3 The Council's Treasury Strategy, including the Annual Investment Strategy and Prudential Indicators was approved by Council on 22 February 2018.

1.4 The two key budgets related to the Council's treasury management activities are the amount of interest earned on investments £240k (£165k General Fund, £75k HRA) and the amount of interest paid on borrowing £2.862m (£75k General Fund, £2.787m HRA).

2. The Report

Interest Rates and Market Conditions

2.1 The Council's treasury advisors Link summarised the key points associated with economic activity in 2018/19 as follows:

- Brexit negotiations have been a focus of much attention during the year;
- UK growth in 2018 was weak initially and then strengthened during the year before falling again in the final quarter;
- As expected the MPC raised Bank Rate from 0.50% to 0.75% on 2 August 2018;
- No further rate rises were expected until uncertainties regarding Brexit were resolved; and
- CPI inflation was on a falling trend throughout the year;

2.2 Deposit rates at the start of 2018/19 have gradually increased, as the rate increases in Q3 17/18 and Q2 18/19 have filtered through into investments placed by the pooled Treasury Fund. As expected, there were no further base rate increases during the final quarter, with the final outturn position of £519k being close to the Q3 forecast of £491k.

Borrowing and Investment Rates in 2018/19

2.3 The movement in relevant UK market interest rates for the year was as follows:

a) For Bank rate

	%
From 1 April 2018 to 1 August 2018	**0.50**
From 2 August 2018 to 31 March 2019	**0.75**

b) For PWLB rates (inclusive of the 0.2% discount rate)

Item	Range during Year %	Start of Year %	End of Year %	Average In Year %
Fixed Interest Maturity				
1 year	1.28 – 1.64	1.48	1.48	1.50
5 years	1.50 – 2.07	1.84	1.55	1.80
10 years	1.80 – 2.50	2.22	1.85	2.19
25 years	2.33 – 2.93	2.55	2.40	2.65
50 years	2.16 – 2.79	2.27	2.23	2.46

c) For Investment rates

The average return to Q4 2018/19 of 0.81% compares with the average benchmark returns as follows:

Item	Range during Year	Start of Year	End of Year	Average during Year
	%	%	%	%
7 day LIBID	0.35 – 0.59	0.36	0.57	0.51
1 month	0.37 – 0.61	0.39	0.61	0.54
3 month	0.48 – 0.81	0.59	0.72	0.68
6 month	0.59 – 0.92	0.70	0.83	0.79
1 year	0.75 – 1.06	0.88	0.94	0.94

Annual Investment Strategy

2.4 The Annual Investment Strategy outlines the Council's investment priorities which are consistent with those recommended by DCLG and CIPFA:

- Security of Capital and
- Liquidity of its investments

2.5 The Investment of cash balances of the Council are managed as part of the investment pool operated by North Yorkshire County Council (NYCC). In order to facilitate this pooling, The Council's Annual Investment strategy and Lending List has been aligned to that of NYCC.

2.6 NYCC continues to invest in only highly credit rated institutions using the Link suggested creditworthiness matrices which take information from all the credit ratings agencies. Officers can confirm that the Council has not breached its approved investment limits during the year.

2.7 The Council’s investment activity in the NYCC investment pool up to Q4 2018/19 was as follows:-

- Balance invested at 31 March 2019 £52.62m
- Average Daily Balance Q4 18/19 £63.41m
- Average Interest Rate Achieved Q4 18/19 0.81%

Borrowing

2.8 It is a statutory duty for the Council to determine and keep under review its “Affordable Borrowing Limits”. The Council’s approved Prudential Indicators (affordable limits) were outlined in the Treasury Management Strategy Statement (TMSS). A list of the limits is shown at Appendix A. Officers can confirm that the Prudential Indicators were not breached during the year.

2.9 The TMSS indicated that there was no requirement to take long term borrowing during 2018/19 to support the budgeted capital programme. However, the borrowing requirement is largely dependent on the Housing Development Programme and whilst it is expected that this will be funded by internal borrowing, this will continue to be reviewed.

2.10 The Council approved an Authorised Borrowing Limit of £84m (£83m debt and £1m Leases) and an Operational Borrowing Limit of £79m (£78m debt and £1m Leases) for 2018/19.

2.11 The strategy, in relation to capital financing, is to continue the voluntary set aside of Minimum Revenue Provision (MRP) payments from the HRA in relation to self-financing debt in order to create capacity to internally borrow to support the Housing Delivery Programme. £1.26m is budgeted for 2018/19 but actual borrowing is currently deferred.

2.12 As a result, the Council was in an under-borrowed position of £99k as at 31 March 2019. This means that capital borrowing is currently below the Council’s underlying need to borrow. The reduction compared to the start of the financial year is the net impact of in-year HRA Voluntary MRP and new capital expenditure in relation to the Housing Delivery Programme, as planned.

2.13 The 2018/19 Treasury Management Strategy forecast an under-borrowed position by the end of 18/19, rising to £14.5m by the end of 20/21 as loans are made to support the Housing Trust, and HRA Housing Investment Programme. Plans to undertake any additional long term borrowing in the short/medium term will be kept under review as the Extended Housing Delivery Programme progresses and while borrowing rates remain low

Capital Strategy

2.14 The Capital Strategy was included as part of the Council's Annual Treasury Management and Investment Strategy 2018/19, approved in February 2018. The Capital Strategy sets out how capital expenditure, capital financing and treasury management contribute to the provision of Corporate and service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability. It sets out the long term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes.

2.15 Alternative non-treasury investments are considered as part of the Capital Strategy. Given the technical nature of potential alternative investments and strong linkages to the Council's Treasury Management function, appropriate governance and decision making arrangements are needed to ensure robust due diligence in order to make recommendations for implementation. As a result, all investments are subject to consideration and where necessary recommendations of the Executive.

2.16 In addition to loans to Selby & District Housing Trust to support the Housing Deliver Programme, options for alternative investments currently being explored are Commercial Property investments, which will be subject to individual business case approval, and Property Funds.

2.17 **Housing Delivery Programme Loans**

The Housing Delivery Programme has delivered a number of successful schemes so far, in partnership with Selby & District Housing Trust. One of the principals underpinning the programme is financial support will be provided to the Trust by way of grant and loans to fund provision of affordable homes in the District whilst achieving a revenue return for the Council's General Fund. The table below summarises the loans provided to date.

Scheme	**Loan Rate %**	**Principal Outstanding £**	**Interest 18/19 £**
Kirgate, Tadcaster	4.56%	190,326	9,240
St Joseph's St	4.20%	313,786	8,904
Jubliee Close, Ricall	3.55%	553,225	- *'
Ulleskelf	4.87%	1,080,060	- *'
Ousegate	3.65%	114,000	- *'
Total Principal / Average Rate	**4.36%**	**2,251,396**	**18,144**

* First instalments due in 2019/20

Commercial Property Investments

2.18 To date there have been two successful bids on Commercial Properties, one in Selby town and one in Tadcaster, both buildings are ex-Natwest Bank Properties. The first successful bid was placed for the Tadcaster property, which completed during Q2 18/19. The second in Selby, which completed towards the end of Q3 18/19. Business cases are currently being developed for the on-going use of the buildings, which means that costs relating to managing the properties, such as Business Rates, security etc. will need to be funded through the Programme for Growth budget until an income stream is generated or the properties are sold on. During 2018/19 cost of £8.6k were incurred.

Property Funds

2.19 On 6th September 2018, The Executive approved exemption of the Council's procurement rules to invest £5m in Property funds, which have been selected through a procurement exercise carried out by the NYCC Treasury Team, in conjunction with the Council's joint treasury advisors, Link, who were commissioned to support the selection process.

2.20 Throughout September and October, the Treasury team carried out the complex application process to buy into the secondary market of Blackrock and Threadneedle Funds, to place £2.5m per fund, direct investment on behalf of SDC. This included application under Mifid II[1] * regulations as the holdings will be wholly owned by SDC. The units were purchased on 31 October 2018.

2.21 The initial investment in both Property Funds incurred total fund entrance fees of £76k – these costs have been charged to the revenue budget in year. The combined opening value of the units was £4.94m.

2.22 Investments held in Property Funds are classified as Non-Specified Investments and are, consequently, long term in nature. Valuations can, therefore, rise as well as fall, over the period they are held. Any gains or losses in the capital value of investments are held in an unusable reserve on the balance sheet and do not impact on the General Fund until units in the funds are sold. Both funds have experienced minor capital losses to the end of March 2019.

2.23 Each fund also provides a monthly revenue return, representing interest earned on the fund over that period. The position on Property Funds at

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[1] *Investment firm" under the Markets in Financial Instruments Directive (MiFID) means "any legal person whose regular occupation or business is the provision of one or more investment services to third parties and/or the performance of one or more investment activities on a professional basis" (Article 4(1)).*

The MiFID definition, therefore, covers all natural and legal persons who perform investment services and activities using financial instruments, as a regular occupation or business, and on a professional basis.

31 March 2019 is as follows:-

Fund	Investment £k	Valuation as at 31-Mar-19 £k	Capital Gain / (Loss) £k	Capital Gain / (Loss) %	Revenue Return £k	Revenue Return %	Total Return %
Blackrock	2,502.50	2,491.49	(11.0)	(0.44)	34.73	3.43	2.99
Threadneedle	2,439.24	2,416.03	(23.2)	(0.93)	47.74	4.84	3.92
Total	**4,941.73**	**4,907.52**	**(34.2)**	**(0.69)**	**82.5**	**4.13**	**3.43**

3. Alternative Options Considered

3.1 Not Applicable.

4.0 Implications

4.1 Legal Implications

There are no legal issues as a result of this report.

4.2 Financial Implications

4.2.1 The Councils investment income during the year has been highlighted through in-year monitoring and is reported in the surplus outturn position for the General Fund and HRA.

4.2.3 Fund entry fees came in lower than anticipated at £76k on the secondary market, which includes frees from the Broker and Link, funded by year one revenue income, generating a net saving in year 1 of £6.5k. If the trend continues into 2019/20, it is expected the funds will generate income of circa £200k per year.

5. Conclusion

5.1 The impact of the economy and Brexit negotiations continue to create uncertainty in the financial markets. Whilst returns remain relatively modest, the council has performed well against benchmark returns whilst maintaining security of the council's cash balances. The property fund investments have provided an additional boost to overall returns, expected to continue over the coming years.

5.2 The Council's debt position is in line with expectations set out in the Strategy, with no immediate changes on the horizon. However, as the Housing Delivery programme progresses and interest rates begin to rise, opportunities to optimise the Council's debt portfolio will be kept under review.

5.3 The Council operated within approved Strategy Indicators for the quarter, with no breaches on authorised limits. The Prudential Indicators are reviewed annually as part of the Treasury Strategy to ensure approved boundaries remain appropriate; activities to date during 18/19 have not highlighted any concerns.

6. Background Documents

Finance Treasury Management Files

Contact Details
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Appendices:
Appendix A – Prudential Indicators as at 31 March 2019