SELBY DISTRICT COUNCIL

Report Reference Number: E/20/4

To:	**Executive**
Date:	**2 July 2020**
Status:	**Non Key Decision**
Ward(s) Affected:	**All**
Author:	**Michelle Oates, Senior Accountant**
Lead Executive Member:	**Councillor Cliff Lunn, Lead Executive Member for Finance and Resources**
Lead Officer:	**Karen Iveson, Chief Finance Officer, S151**

Title: Treasury Management – Annual Review 2019/20

Summary:

This report reviews the Council's borrowing and investment activity (Treasury Management) for the period 1st April 2019 to 31 March 2020 and presents performance against the Prudential Indicators.

Investments – On average the Council's investments held in the NYCC investment pool totalled £66.04m over the year at an average rate of 0.91% and earned interest of £601k (£415k allocated to the General Fund; £186k allocated to the HRA) which is £166k above the total annual budget. This exceeded estimates at Q3, which remained prudent in the event that Brexit would result in a sharp decline in rates. For the General Fund £65k interest earned above a £350k threshold is to be transferred to the Contingency Reserve.

In addition to investments held in the pool, the council has £4.69m invested in property funds as at 31 March 2020. The funds achieved 3.46% revenue return and 4.54% capital loss. This resulted in revenue income of £168.9k to the end of Q4 and an 'unrealised' capital loss of £222.8k. These funds are long term investments and changes in capital values are realised when the units in the funds are sold.

Borrowing – Long-term borrowing totalled £59.3m at 31 March 2020, (£1.6m relating to the General Fund; £57.7m relating to the HRA), Interest payments of £2.5m were paid 2019/20, a saving of £0.3m against budget. The Council undertook no short term borrowing in year.

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

Looking ahead to 2020/21 investment returns are expected to be significantly lower as a result of the cut in Bank Base Rate to 0.1%, in response to the economic challenges arising from the Covid-19 global pandemic. No changes to the Treasury

Management Strategy are proposed but revised forecasts will inform a revised budget for 2020/21 and the next refresh of the Medium-Term Financial Strategy.

Recommendations:

I. **Councillors endorse the actions of officers on the Council's treasury activities for Q4 2019/20 and approve the report.**

II. **Note general fund investment income received over the £350k threshold to be transferred to contingency reserve, equating to £65k 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 2019/20 and covers the period 1 April 2019 to 31 March 2020. 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 21 February 2019.

1.4 The two key budgets related to the Council's treasury management activities are the amount of interest earned on investments £435k (£300k General Fund, £135k HRA) and the amount of interest paid on borrowing £2.788m (£75k General Fund, £2.713m HRA).

2. The Report

<u>Market Conditions and Interest Rates</u>

2.1 The Council's treasury advisors Link Asset Services – Treasury Solutions summarised the key points associated with economic activity in 2019/20 up to 31 March 2020**:**

- the focus in the House of Commons was to agree a way forward for the UK over Brexit;
- the general election in December enabled the UK to leave the EU on 31 January 2020;

- the uncertainties around Brexit, resulted in the MPC maintaining Bank Rate at 0.75% until March 2020 when two emergency cuts in Bank Rate from 0.75% to 0.25% and then to 0.10% were made as a result of the coronavirus outbreak. These cuts were accompanied by an increase in quantitative easing (QE), essentially the purchases of gilts (mainly) by the Bank of England of £200bn, and
- the Government introduced various schemes to subsidise both employed and self-employed jobs for three months while the country is locked down due to the coronavirus outbreak. It also put in place other measures to help businesses access loans from their banks, (with the Government providing guarantees to the banks against losses)

Interest Rate Forecasts

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

a) for Bank rate

Period	%
1 April 2019 – 10 March 2020	0.75
11 March 2020 – 18 March 2020	0.25
19 March 2020 – 31 March 2020	0.10

b) for PWLB rates

Item	Range during Year	Start of Year	End of Year	Average In Year
	%	%	%	%
Fixed Interest Maturity				
1 year	1.17 - 2.47	1.46	1.90	1.70
5 years	0.99 - 2.48	1.55	1.96	1.98
10 years	1.15 - 2.79	1.88	2.17	2.23
25 years	1.73 - 3.25	2.41	2.65	2.76
50 years	1.57 - 3.05	2.24	2.38	3.60

* Net of certainty rate 0.2% discount

c) for Investment rates

Deposit rates continued into the start of 2019/20 at previously depressed levels and the fell sharply following the cut to base rate in March 2020, in response to the Covid-19 global pandemic.

Item	Range during Year	Start of Year	End of Year	Average during Year
	%	%	%	%
7 day LIBID	0.00 – 0.58	0.56	0.00	0.53
1 month	0.11 – 0.61	0.60	0.12	0.56
3 month	0.26 – 0.72	0.72	0.47	0.63
6 month	0.31 – 0.83	0.83	0.60	0.70
1 year	0.39 – 0.98	0.94	0.74	0.80

Annual Investment Strategy

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

2.4 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 Councils Annual Investment strategy and Lending List has been aligned to that of NYCC.

2.5 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.

2.6 The Council's investment activity in the NYCC investment pool up to 31 March 2020 was as follows:-

- Balance invested at 31 March 2020 £66.66m
- Average Daily Balance Q4 19/20 £66.04m
- Average Interest Rate Achieved Q4 19/20 0.91%

2.7 Looking ahead to 2020/21 investment returns are expected to be significantly lower as a result of the cut in Bank Base Rate to 0.1%, in response to the economic challenges arising from the Covid-19 global pandemic. No changes to the Treasury Management Strategy are proposed but revised forecasts will inform a revised budget for 2020/21 and the next refresh of the Medium-Term Financial Strategy.

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 2019/20 to support the budgeted capital programme. However, the borrowing requirement is largely dependent on the Housing Development Programme and whilst it is currently expected that this will be funded by internal borrowing in the short term, this will continue to be reviewed.

2.10 The Council approved an Authorised Borrowing Limit of £90m (£89m debt and £1m Leases) and an Operational Borrowing Limit of £85m (£84m debt and £1m Leases) for 2019/20.

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 be in a position to repay the debt over 30 years. £1.26m was budgeted for 2019/20 and has been set aside.

2.12 As a result, the Council was in an over-borrowed position of £5.3m as at 31 March 2020. This means that capital borrowing (external debt) is currently and temporarily in excess of the Council's underlying need to borrow. The increase of £563k compared to the 2018/19 year-end position is a result of the in-year HRA self-financing set aside offset by Capital expenditure. Planned capital expenditure funded by prudential borrowing, will increase the Council's capital financing requirement.

2.13 The 2019/20 Treasury Management Strategy forecast an under-borrowed position of £12.4m by the end of 21/22 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 2019/20, approved in February 2019. 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 Delivery Programme, options for alternative investments currently being pursued are Commercial Property investments, which are subject to individual business case approval, and Property Funds.

Housing Delivery Programme Loans

2.17 The Housing Delivery Programme has delivered a number of successful schemes so far, in partnership with Selby & District Housing Trust. One of the principles 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 19/20 £
Kirgate, Tadcaster	4.56%	190,326	9,071
St Joseph's St	4.20%	206,418	8,875
Jubliee Close, Ricall	3.55%	558,126	19,669
Ulleskelf	4.87%	1,074,470	51,824
Ousegate	3.65%	883,424	25,089
Total Principal / Average Rate	**4.19%**	**2,912,763**	**114,527**

Commercial Property Investments

2.18 To date there have been acquisitions of Commercial Properties, one in Selby town and one in Tadcaster, both buildings are ex-Natwest Bank Properties. Proposals for onward sale and development are in progress.

Property Funds

2.19 The position on Property Funds at 31 March 2020 is as follows:

In Year Performance -

			In Year Performance Q4 19/20			
Fund	**Bfwd Investment £k**	**Valuation as at 31-Mar-20 £k**	**Capital Gain / (Loss)**		**Revenue Return**	
			£k	**%**	**£k**	**%**
Blackrock	2,491.49	2,376.60	(114.9)	(4.61)	85.4	3.45
Threadneedle	2,416.03	2,308.11	(107.9)	(4.47)	83.5	3.48
Total	**4,907.52**	**4,684.70**	**(222.8)**	**(4.54)**	**168.9**	**3.46**

Total Fund Performance

Fund	Original Investment £k	Valuation as at 31-Mar-20 £k	Total Performance			
			Capital Gain / (Loss)		Revenue Return	
			£k	%	£k	%
Blackrock	2,502.50	2,376.60	(125.9)	(5.03)	120.1	3.44
Threadneedle	2,439.24	2,308.11	(131.1)	(5.38)	161.2	4.76
Total	**4,941.73**	**4,684.70**	**(257.0)**	**(5.20)**	**281.4**	**4.09**

2.20 Investments held in Property Funds are classified as Non-Specified Investments and are, consequently, long term in nature. Valuations can, therefore, fall and rise 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. These funds are intended to be held for the longer term (5 years initially) in order to mitigate the risk of shorter-term losses.

2.21 Despite the uncertainty relating to the economy, the UK property market has been relatively robust. Whilst experiencing some capital value loss, both funds have delivered positive revenue returns and a net positive return overall prior to March 2020.

2.22 Since March 2020 the impact of Covid-19 is causing volatility across all investment markets globally, as such major property valuation firms and their professional body (RICS) concluded unprecedented circumstances on which to base valuation judgement and were thus required to include a 'Material Valuation Uncertainty' clause to their valuations as at 31 March 2020. Both funds experienced a sharp decline in capital value in March 2020, resulting in a net overall loss across both funds. Property Fund investments in particular are expected to be impacted by the uncertainty within the economy in the short term and there is potential for further reductions in capital values and revenue returns. The Statements have been issued to state the funds assets will be kept under regular review.

2.23 These investments are intended to be longer term in nature and the Council's strong financial position enabled the investment to be funded from reserves. This means future spending plans and cash balances are not reliant on access to the principal sums invested, and therefore may be held until unit values recover from losses. However, the Property Fund sector and performance of both Property Funds will continue to be monitored with support from Treasury Management advisers, Link.

3. Alternative Options Considered

3.1 The Council has access to a range of investments through the pooled arrangements in place through North Yorkshire County Council.

4. Implications

4.1 Legal Implications

4.1.1 There are no legal implications as a result of this report.

4.2 Financial Implications

4.2.1 The financial implications are set out in the report.

4.3 Policy and Risk Implications

4.3.1 Management of the Council's treasury activities are in accordance with approved policies. Treasury management in Local Government is governed by the CIPFA "Code of Practice on Treasury Management in the Public Services" which aims to ensure 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.

4.4 Corporate Plan Implications

4.4.1 There are no direct Corporate Plan implications as a result of this report.

4.5 Resource Implications

4.5.2 The resources necessary to manage the Council's Treasury activities are contained within the collaboration agreement with NYCC.

4.6 Other Implications

4.6.1 There are no other implications as a direct result of this report.

4.7 Equalities Impact Assessment

4.7.1 There are no equalities impacts as a direct result of this report

5. Conclusion

5.1 Overall the Council's investments have performed relatively well over the year and returns have exceeded budget. However the cut in Bank Base Rate in March 2020 in response to the Covid-19 pandemic will mean a significant reduction in returns for the foreseeable future and uncertainty ahead.

5.2 Property Fund investments in particular are expected to be impacted by the uncertainty within the economy in the short term and there is potential for further reductions in capital values and revenue returns. The investments are intended to be longer term in nature and the Council's strong financial

position enabled the investment to be funded from reserves. This means future spending plans and cash balances are not reliant on access to the principal sums invested, and therefore may be held until unit values recover from losses.

5.3 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.

5.4 The Council operated within approved Strategy Indicators for the year, 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 2019/20 have not highlighted any concerns.

5.5 The impact of the economy, and the turmoil in the financial markets, continues to have an impact on the Council's investment returns. Unprecedented events since the outbreak of Covid-19 leads to further uncertainty around future returns. No changes to the Treasury Management Strategy are proposed at this stage, but revised forecasts will inform a revised budget for 2020/21 and the next refresh of the Medium-Term Financial Strategy.

6. Background Documents

None

7. Appendices:

Appendix A – Prudential Indicators as at 31 March 2020

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