Inverclyde council

AGENDA ITEM NO: 9

Report To:	**Inverclyde Council**	**Date:**	**5 December 2019**
Report By:	**Corporate Director Environment, Regeneration & Resources**	**Report No:**	**RMcG/LP/139/19**
Contact Officer:	**Rona McGhee**	**Contact No:**	**01475 712113**
Subject:	**Treasury Management – Mid-Year Report 2019/20: Remit from Policy & Resources Committee**		

1.0 PURPOSE

1.1 The purpose of this report is to request the Council to consider a remit from the Policy & Resources Committee.

2.0 SUMMARY

2.1 The Policy & Resources Committee at its meeting on 19 November 2019 considered a report by the Chief Financial Officer on the operation of the treasury function and its activities for the first six months of 2019/20 as required under the terms of Treasury Management Practice 6 ('TMP6') on 'Reporting Requirements and Management Information Arrangements'.

2.2 A copy of the report to the Policy & Resources Committee is attached as Appendix 1.

2.3 The Policy & Resources Committee decided:
(1) that the contents of the Mid-Year Report on Treasury Management for 2019/20 and the ongoing work to ensure the delivery of financial benefits for the Council be noted;
(2) that approval be given to the Prudential Repayment policy for Loan Charges principal repayments as shown in Appendix 3 and that the £1,400,000 one-off and £400,000 recurring saving generated by the Loan Charges review be noted; and
(3) that the Mid-Year Report be remitted to the Inverclyde Council for approval.

3.0 RECOMMENDATION

3.1 The Council is asked to approve the Treasury Management Mid-Year Report 2019/20.

Gerard Malone
Head of Legal & Property Services

APPENDIX

Inverclyde council

AGENDA ITEM NO.

Report To:	**Policy & Resources Committee**	**Date:**	**19 November 2019**
Report By:	**Chief Financial Officer**	**Report No:**	**FIN/104/19/AP/KJ**
Contact Officer:	**Alan Puckrin**	**Contact No:**	**01475 712223**
Subject:	**TREASURY MANAGEMENT – MID-YEAR REPORT 2019/20**		

1.0 PURPOSE

1.1 The purpose of this report is to advise Members of the operation of the treasury function and its activities for the first six months of 2019/20 as required under the terms of Treasury Management Practice 6 ("TMP6") on "Reporting Requirements and Management Information Arrangements".

2.0 SUMMARY

2.1 As at 30 September 2019 the Council had gross external debt (including PPP) of £275,414,731 and investments (cash balances managed in house) of £32,938,024. This compares to gross external debt (including PPP) of £259,326,319 and investments of £18,915,222 at 31 March 2019. The movements are largely due to PWLB borrowing undertaken to provide funding for forthcoming requirements and financing maturing debt/liabilities (including £10m of PWLB borrowing which was due for repayment in October 2019).

2.2 The Council is projected to be underborrowed by £29,488,000 compared to its Capital Financing Requirement as at 31 March 2020. This is a decrease of £4,876,000 from the estimate of £34,364,000 in the 2019/20 Treasury Management Strategy. The under borrowing position means that the Council is using funds it currently has (such as reserves) to cash flow capital expenditure rather than bringing in new funds from borrowing.

2.3 The Council undertook a total of £22,000,000 of PWLB borrowing and £3,000,000 of temporary borrowing during the period. The temporary borrowing (from an English local authority and for cash flow purposes) has been repaid whilst £15,000,000 of the PWLB borrowing is being used to repay maturing debt. The projection for the remainder of the year includes a further £8,000,000 of borrowing that will only be undertaken if the funds are required and it is prudent to borrow. Any borrowing undertaken will be reported to the Committee.

2.4 The average rate of return achieved on investments during the first six months of 2019/20 was 0.82% which exceeds the benchmark return rate for the period of 0.66% by 0.16% and resulted in £15,700 of additional interest on investments for the Council.

2.5 During the first six months of 2019/20 the Council did not undertake any debt restructuring and operated within the required treasury limits and Prudential Indicators for the year set out in the Council's Treasury Policy Statement, annual Treasury Strategy Statement, and the Treasury Management Practices.

2.6 On 9 October the PWLB announced an immediate and unexpected 1% increase in interest rates for new borrowing. It is likely that decision will lead to further lenders seeking to provide funding to Councils at lower rates than the PWLB offer or to an increase in short-term borrowing.

2.7 A review has been undertaken of the periods over which previous years' capital expenditure is being written-off to revenue as part of the Loan Charges budget. Following the review, a Prudential Repayment policy has been prepared (Appendix 3) and Committee approval is being sought to adopt this policy.

2.8 The Loan Charges review identified projects where the write-off periods currently being used should be amended to more closely match the expected life of the assets involved, in line with the proposed Prudential Repayment policy. This has resulted in a £1,400,000 saving in Loan Charge principal repayments for the period to 31 March 2019 which will be allocated to the Loan Charges Earmarked Reserve. There will also be ongoing Loan Charge repayment savings of £400,000 per year from 2019/20 through to 2035/36, following which repayments will increase as a result of the extension of the write-off periods to bring those periods more in line with the asset lives. This saving will help reduce the funding gap in 2020/21.

3.0 RECOMMENDATIONS

3.1 It is recommended that the Committee notes the contents of the Mid-Year Report on Treasury Management for 2019/20 and the ongoing work to ensure the delivery of financial benefits for the Council.

3.2 It is recommended that the Committee approves the Prudential Repayment policy for Loan Charges principal repayments as shown in Appendix 3 and notes the £1,400,000 one-off and £400,000 recurring saving generated by the Loan Charges review.

3.3 It is recommended that the Mid-Year Report be remitted to the Inverclyde Council for approval.

Alan Puckrin
Chief Financial Officer

4.0 BACKGROUND

4.1 The Council is required by the CIPFA Code of Practice on Treasury Management 2011 and the CIPFA Prudential Code for Capital Finance in Local Authorities to produce a mid-year treasury management review of activities and prudential and treasury indicators for 2019/20.

4.2 Treasury Management in this context is defined as: “The management of the local authority’s 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.”

5.0 MID-YEAR REVIEW

5.1 The treasury management issues arising during the first six months of 2019/20 were:

a. The Council’s debt (including PPP) has increased during the period by £16,088,412 due to borrowing undertaken to provide funding for forthcoming requirements and financing maturing debt/liabilities (including £10,000,000 of PWLB borrowing which was due for repayment on 14 October 2019).

b. The Council’s investments have increased by £14,022,802 due to borrowing (see item h. below) and from regular cash flow movements.

c. As at 31 March 2019 the Council had under borrowed against its capital financing requirement by £48,136,000. The latest projection is for the under borrowing to reduce to £29,488,000 as at 31 March 2020. Under borrowing means that the Council is using funds it currently has to cash flow capital expenditure rather than bringing in funds from borrowing. The projected level of under borrowing is considered manageable but the position is kept under review in light of Council capital financing and other funding requirements.

d. There remains ongoing volatility in the financial markets and economic uncertainty in the UK and around the world, impacting on rates for new borrowing and investments. The UK Bank Rate has remained unchanged at 0.75% since August 2018 but there remains uncertainty over when the next change will take place and if that change will see an increase or decrease in rates.

e. The latest forecast from the Council’s treasury advisers (produced in August) is for no change to the Bank Rate until an increase to 1.00% in Quarter 4 of 2020.

f. During the period PWLB rates for new borrowing had been expected to see slight increases of up to 0.10%. Rates actually fell, largely by around 0.20% to 0.40% for shorter periods and 0.55% to 0.59% for longer borrowing. The volatility during the 6-month period resulted in spreads between the high and low rates for some loan periods of up to 0.96% (e.g. borrowing rates for 12 years of 1.43% at the end of September had been 1.24% earlier in September and at 2.20% in April).

g. On 9 October the PWLB announced an immediate and unexpected 1% increase in interest rates for new borrowing. It is likely that decision will lead to further lenders seeking to provide funding to Councils at lower rates than the PWLB offer or to an increase in short-term borrowing. This decision aside, the Council’s treasury advisers expect PWLB rates to rise very gently during the rest of the year but the extent and speed of increase will depend on economic factors affecting the UK and global markets.

h. During the period the Council undertook the following borrowing:

   a) £2,000,000 from PWLB at 2.21% in April 2019 for 43½ years. The borrowing was at a reduced Local Infrastructure Rate allocated for individual projects approved by HM Treasury, in this case the Extension to Gourock Primary School.

   b) £3,000,000 of temporary borrowing at 0.80% between April 2019 and May 2019 from an English local authority. The borrowing was for cash flow purposes and has been repaid.

   c) £20,000,000 from PWLB in September 2019 (£10m at 1.21% for 10 years and £10m at 1.40% for 13 years). This borrowing provided funding for £5m of PWLB debt that matured in July 2019 and £10m that matured in October 2019.

i. The projection for the remainder of the year includes a further £8,000,000 of borrowing that will only be undertaken if the funds are required and it is prudent to borrow. Any borrowing undertaken will be reported to Committee.
j. The Council did not undertake any debt restructuring during the first six months of 2019/20 and remained within its Prudential Indicator and Treasury Management limits.
k. Investment returns were expected to remain relatively low and have remained so during the period.
l. The Council's investments earned a rate of return of 0.82% during the period and outperformed the benchmark return of 0.66% resulting in additional income to the Council of £15,700.
m. All investments were in accordance with the Council's investment policy and no institutions with which investments were made had any difficulty in repaying those investments and interest in full during the period.
n. The Council's investment performance is due to undertaking fixed term investments at interest rates that were above the benchmark with counterparties that have high creditworthiness (the Bank of Scotland and Santander UK) and in accordance with the Council's investment strategy. The outturn is reduced due to having previously used investments to repay maturing debt and thereby saving the Council the cost of borrowing at rates higher than being earned from using investment funds.

5.2 The Council's debt position was as follows:

	At 31 March 2019	At 30 September 2019
	£	£
Total Excluding PPP	196,843,319	213,786,731
PPP Debt	62,483,000	61,628,000
Total Including PPP	259,326,319	275,414,731

Further detail is given in the following table:

	At 31 March 2019		At 30 September 2019		Movement In Period
	Principal	Rate	Principal	Rate	Principal
	£000		£000		£000
Fixed Rate Funding:					
- PWLB	97,260		114,180		16,920
- Market *	56,000		40,000		See * Below
	153,260	3.94%	154,180	3.51%	16,920
Variable Rate Funding:					
- PWLB	0		0		0
- Market *	43,400		59,400		See * Below
- Temporary #	183		207		(26)
	43,583	4.93%	59,607	4.89%	(26)
Total Debt (Excl PPP)	196,843	4.16%	213,787	3.89%	16,894
PPP Debt	62,483		61,628		(855)
Total Debt (Incl PPP)	259,326		275,415		16,039

* - Market Loans are shown as variable when they have less than 1 year to go until their next call date. The total value of Market Loans has not changed between financial years, just the split between fixed and variable.

- Temporary Loans include funds held by the Council on behalf of the Common Good and Trust Funds that are treated as borrowing for Treasury Management purposes.

5.3 The Council's investment position was as follows:

	At 31 March 2019		At 30 September 2019		Movement In Period
	Principal	Return	Principal	Return	Principal
	£000		£000		£000
Investments:					
- Fixed Term Deposits	10,000	1.00%	5,000	0.85%	(5,000)
- Notice Accounts	0	-	5,000	0.95%	5,000
- Deposit Accounts	8,915	0.75%	22,938	0.65%	14,023
Totals	18,915	0.88%	32,938	0.73%	14,023

Maximum level of investments in Period: £41,765,824 on 17 September 2019
Minimum level of investments in Period: £ 7,145,523 on 26 July 2019
Daily average for the period: £19,581,276

An analysis of the above investments is shown in Appendix 1.

In addition to the above cash balances managed in-house, the Council has other transactions/balances required to be treated as investments under Investment Regulation 31. Appendix 2 includes these transactions/balances along with estimates for 2019/20.

5.4 <u>2019/20 Latest Projection Compared to Estimates in 2019/20 Strategy</u>
The latest 2019/20 projection compared to the estimates in the 2019/20 strategy:

	2019/20 Estimate	2019/20 Latest Projection
<u>Borrowing Requirement</u>	£000	£000
New borrowing	5,000	5,000
Alternative financing requirements	0	0
Replacement borrowing	25,000	25,000
TOTAL	30,000	30,000
<u>Prudential/Treasury Management Indicators</u>	£000	£000
Gross external debt including PPP (As at 31 March 2020)	277,456	272,473
Capital financing requirement (As at 31 March 2020)	311,820	301,961
(Under)/over borrowing against CFR	(34,364)	(29,488)
	£000	£000
Gross Capital Expenditure	34,226	22,972
Ratio of financing costs (including PPP) to net revenue stream	14.75%	13.91%
Ratio of net debt (debt and PPP less investments) to net revenue stream	137.0%	128.5%

5.5 2019/20 Mid-Year Position Compared to Limits in 2019/20 Strategy

The 2019/20 mid-year position compared to limits in the 2019/20 strategy:

	2019/20 Limits		2019/20 Mid-Year Actual Position	
Prudential/Treasury Management Indicators				
Authorised limit for external debt	£000		£000	
• Borrowing	249,000		213,787	
• Other long term liabilities	63,000		61,628	
	312,000		275,415	
Operational boundary for external debt	£000		£000	
• Borrowing	239,000		213,787	
• Other long term liabilities	63,000		61,628	
	302,000		275,415	
Upper limit on sums invested for periods longer than 365 days (Actual is maximum in period)	£000 10,000		£000 0	
Upper limits on Fixed/Variable borrowing maturing in each period (LOBOs included based on call dates and not maturity dates) at 31 March 2019	Fixed	Var.	Fixed	Var.
• Under 12 months	45%	35%	7.1%	27.9%
• 12 months and within 24 months	45%	35%	-	-
• 24 months and within 5 years	45%	35%	11.8%	-
• 5 years and within 10 years	45%	35%	5.3%	-
• 10 years and within 30 years	45%	35%	8.2%	-
• 30 years and within 50 years	45%	35%	21.0%	-
• 50 years and within 70 years	45%	35%	18.7%	-
Council Policy Limits				
Maximum Percentage of Debt Repayable In Year	25%		18.7%	
Maximum Proportion of Debt At Variable Rates	45%		27.9%	
Maximum Percentage of Debt Restructured In Year	30%		0.0%	

5.6 The forecast from the Treasury Advisors in the 2019/20 Strategy for the Bank Rate as at 31 March and the latest forecast for the Bank Rate are:

	Forecast Per 2019/20 Strategy	Latest Forecast
2019/20	1.25%	0.75%
2020/21	1.50%	1.00%
2021/22	2.00%	1.25%

5.7 The Council's investment policy for the year is governed by Scottish Government Investment Regulations, which was implemented in the annual investment strategy approved by the Council on 21 February 2019. This policy sets out the approach for choosing investment categories and counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data such as rating outlooks, credit default swaps, bank share prices etc.

5.8 All investments were in accordance with the policy and no institutions with which investments were made had any difficulty in repaying investments and interest in full during the period.

The result of the investment strategy undertaken by the Council in the first six months of 2019/20 is as follows:

Average Investment	Rate of Return (gross of fees)	Benchmark Return (3 month LIBID uncompounded)
£19,581,276	0.82%	0.66%

The Council have outperformed the benchmark by 0.16% resulting in additional income to the Council of £15,700. Opportunities for the Council to out-perform the benchmark rate are becoming fewer due to more standardisation of rates and periods offered.

6.0 LOAN CHARGES REVIEW AND PRUDENTIAL REPAYMENT POLICY

6.1 Following Audit Scotland changes to their advice to applying Scottish Government guidance on Loan Charges earlier this year, a review was undertaken of the periods over which previous years' capital expenditure is being written-off to revenue as part of the Loan Charges budget.

6.2 The purpose of the review has been:

a. To produce a proposed Prudential Repayment policy for capital expenditure for the maximum periods over which that expenditure will be written-off to revenue through Loan Charges. Committee approval is being sought to adopt the policy which is attached as Appendix 3.
b. To identify projects where the write-off periods currently being used should be amended to more closely match the expected life of the assets involved, in line with the proposed Prudential Repayment policy. The projects and changes identified are shown in Appendix 4.

6.3 The financial impact of the review is that:

a. A £1,400,000 saving has been identified in Loan Charge principal repayments for the period to 31 March 2019. This will be credited to the Loan Charges Earmarked Reserve.
b. There will also be ongoing Loan Charge repayment savings of £400,000 per year from 2019/20 through to 2035/36. After this, the Loan Charge principal repayments will increase as a result of the extension of the write-off periods to bring those periods more in line with the asset lives.
c. The reduction in annual Loan Charge principal repayments means that, compared to now and through to 2035/36, the Council's Capital Financing Requirement and the Council's level of under-borrowing will be higher than would have been the case. The Authorised Limit and Operational Boundary will need to be adjusted accordingly.

7.0 IMPLICATIONS

7.1 Legal

None. Any borrowing or lending is done under the Council's legal powers.

7.2 Finance

Through the achievement of exceeding the investment benchmark return rate, the Council has benefited from additional returns of £15,700. The Council utilises Treasury Management as part of the overall Financial Strategy. Officers will continue to investigate borrowing and investment opportunities to bring financial benefits to the Council, all within the Treasury Management Policy.

7.3 **Human Resources**

None.

7.4 **Equalities**

Equalities

(a) Has an Equality Impact Assessment been carried out?

	YES (see attached appendix)
X	NO – This report does not introduce a new policy, function or strategy or recommend a substantive change to an existing policy, function or strategy. Therefore, no Equality Impact Assessment is required

(b) Fairer Scotland Duty

If this report affects or proposes any major strategic decision:-

Has there been active consideration of how this report's recommendations reduce inequalities of outcome?

	YES – A written statement showing how this report's recommendations reduce inequalities of outcome caused by socio-economic disadvantage has been completed.
X	NO

(c) Data Protection

Has a Data Protection Impact Assessment been carried out?

	YES – This report involves data processing which may result in a high risk to the rights and freedoms of individuals.
X	NO

7.5 **Repopulation**

None.

8.0 CONSULTATIONS

8.1 This report has been produced based on advice from the Council's treasury advisers (Link Treasury Services Limited).

9.0 LIST OF BACKGROUND PAPERS

9.1 CIPFA - Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes – 2017 Edition
Inverclyde Council – Treasury Management Strategy and Annual Investment Strategy 2019/20-2022/23.

CASH BALANCES MANAGED IN-HOUSE
ACTUAL AS AT 31 MARCH 2019 AND 30 SEPTEMBER 2019

The following is an analysis of cash balances managed in-house as at 31 March 2019 and at 30 September 2019:

	As At 31 March 2019	**As At 30 September 2019**
	£	£
Fixed Term Deposits		
Bank of Scotland	10,000,000	5,000,000
Santander UK	0	0
	10,000,000	5,000,000
Average Interest Rate	1.00%	0.85%
Notice Accounts		
Bank of Scotland	0	5,000,000
Santander UK	320	321
	320	5,000,321
Average Interest Rate	0.60%	0.95%
Deposit Accounts		
Bank of Scotland	8,914,400	22,937,200
Santander UK	502	503
	8,914,902	22,937,703
Average Interest Rate	0.75%	0.65%
TOTAL	18,915,222	32,938,024
Average Interest Rate	0.88%	0.73%

<u>**Appendix 2**</u>

FORECAST OF INVESTMENT BALANCES
ESTIMATE FOR 2019/20 AND ACTUAL AT 30 SEPTEMBER 2019

Investment Regulation 31 requires the Council to provide forecasts for the level of investments. The estimate for 2019/20 and the actual as at 30 September 2019 are:

	2019/20	**2019/20**
	Estimate For Year	**Actual For 1 April 2019 To 30 September 2019**
	£000	£000
Cash balances managed in-house		
- At Start of Year	25,000	18,915
- At End of Year/Period	19,426	32,938
- Change in Year/Period	(5,574)	14,023
- Average daily cash balances	22,213	19,581
Holdings of shares, bonds, units (includes local authority owned company)		
- At Start of Year	2	2
- Purchases	0	0
- Sales	0	0
- At End of Year/Period	2	2
Loans to local authority company or other entity to deliver services		
- At Start of Year	483	483
- Advances	0	0
- Repayments	42	19
- At End of Year/Period	441	465
Loans made to third parties (Largely BPRA) #		
- At Start of Year	2,128	2,139
- Advances	0	4
- Repayments	22	13
- At End of Year/Period	2,106	2,129
Total of all investments		
- At Start of Year	27,613	21,539
- At End of Year/Period	21,975	35,534
- Change in Year/Period	(5,638)	13,995

- This includes the £50,000 investment made with the Shared Interest Society Limited in August 2017.

Appendix 3

LOAN CHARGE PRINCIPAL REPAYMENTS
PROPOSED PRUDENTIAL REPAYMENT POLICY

1. The maximum repayment periods for capital expenditure:
   a. Computers/Network Equipment
      - Software 5 years
      - PCs 6 years
      - Servers 7 years
   b. Vehicles
      - 5 years or 7 years depending on type of vehicle
   c. 3G Pitches
      - Up to 15 years
   d. Repairs and Renewal Work (e.g. Window Replacement, Reroofing)
      - 20 years
   e. Roads Carriageway Upgrades
      - 20 to 25 years
   f. Footway Upgrades
      - 30 years
   g. Major Refurbishment Work
      - 30 years
   h. New Buildings (including schools)
      - 40 years
   i. Major Regeneration Works
      - 60 years
   j. Purchase of Land
      - 100 years
   k. Development Sites
      - 100 years

2. The repayment periods for individual items are to be applied on a prudent basis and be based on the expected useful life of the assets/expenditure involved.

3. Repayments are currently calculated using the annuity method (in which repayments increase each year during the write-off period). This method has been used for many years and will be used for calculating repayments on capital expenditure incurred up to 2020/21. For new capital expenditure from 2021/22 onwards, the Council is required to select its calculation method from options set by the Scottish Government. Of those available, it is proposed to use the equal instalment method (where repayments start higher than under the annuity method but do not change during the write-off period).

Finance Services,
October 2019.

Appendix 4

LOAN CHARGE REVIEW
CHANGES TO PERIODS CURRENTLY BEING USED, IN LINE WITH PROPOSED POLICY

The main projects and changes identified from the Loan Charges review are:

Project	Write-Off Period Adjustment (Years)
a. Depots AMP	From 20 to 40
b. Offices AMP	From 20 to 30
c. Gourock Central Development	From 20 to 60
d. Broomhill Regeneration	From 20 to 60
e. Clune Park Regeneration	From 20 to 100
f. Leisure Strategy	From 30 to 40

These changes are being made to more closely match the expected life of the assets involved, in line with the proposed Prudential Repayment policy.