

Cherwell District Council

Accounts, Audit and Risk Committee

18 March 2020

Treasury Management Report – Q3 2019/20

Report of the Director of Finance

This report is public

Appendix 1 is exempt from publication by virtue of paragraph 3 of Schedule 12A of Local Government Act 1972

Purpose of report

To receive information on treasury management performance and compliance with treasury management policy for 2019/20 as required by the Treasury Management Code of Practice.

1.0 Recommendations

The meeting is recommended:

- 1.1 To note the contents of the December 2019 Treasury Management Report.

2.0 Introduction

- 2.1 In 2012 the Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Council to approve treasury management semi-annual and annual reports.
- 2.2 The Council's treasury management strategy for 2019/20 was approved at a meeting on 25 February 2019. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk is therefore central to the Council's treasury management strategy.
- 2.3 Following consultation in 2017, CIPFA published new versions of the Prudential Code for Capital Finance in Local Authorities (Prudential Code) and the Treasury Management Code of Practice; the local authority specific Guidance Notes for the Codes were published in July 2018. In England MHCLG published its revised Investment Guidance which came into effect from April 2018.
- 2.4 The updated Prudential Code includes a new requirement for local authorities to provide a Capital Strategy, which is to be a summary document approved by full

Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 25 February 2019.

3.0 Report Details

2019/20 Performance

- 3.1 As at the end of December 2019 the Council had borrowing of £123m and investments of £41m – a net borrowing position of £82m. Appendix 1 details the schedule of borrowing and investments as at 31 December 2019.

Strategy

- 3.2 The Treasury Management Strategy for 2019/20 includes the Annual Investment Strategy which sets out the Council's investment priorities. Security of capital has remained the Council's main investment objective, followed by liquidity of capital, and then by yield. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2019/20.
- 3.3 Counterparty credit quality is assessed and monitored with reference to:
- Credit Ratings - the Council's minimum long-term counterparty rating of A- (or equivalent) across rating agencies Fitch, S&P and Moody's
 - Credit default swaps – a type of insurance to protect against default risk
 - GDP of the country in which the institution operates
 - The country's net debt as a percentage of GDP
 - Sovereign support mechanisms or potential support from a well-resourced parent institution
 - Share price
- 3.4 The Arlingclose ratings and advice encompass all of these and other factors and is the Council's primary source of guidance in selecting investments. In addition to Arlingclose ratings and advice, the council keeps an internal counterparty 'Watch List' based on intelligence from a variety of other sources available to officers.
- 3.5 The Council's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective.
- 3.6 In furtherance of these objectives new borrowing was kept to a minimum, whilst options for securing lower rates for longer term borrowing were reviewed, as part of an ongoing process. This strategy enabled the Council to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.
- 3.7 All treasury management activities undertaken during the first 9 months of 2019/20 complied with the CIPFA Code of Practice and the Council's approved Treasury Management Strategy, and all indicators were met during, and at the end of, the reporting period.

Investment performance for 9 months ended 31 December 2019:

- 3.8 Investment rates available in the market have continued at low levels, with the Bank of England Base rate remaining at 0.75% since August 2018.

Funds available for investment are on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and funding of the Capital Programme.

- 3.9 The table below shows the investment position during and at the end of the reporting period:

	Investment Amount £	Interest Rate	Interest Budget £	Interest Actual £	Variance £
Apr-Dec 2019	£33.2m (average)	0.69% (annualised)	115k	172k	57k
As at 31/12/19	£41.1m	0.66%	-	-	-

Rate Benchmarking	Overnight	7-day	1-month
LIBOR	0.67%	0.69%	0.72%
SONIA (Mid-rate)	0.71%	0.77%	0.75%

Interest receivable is currently ahead of target, and is forecast to remain above budget at the end of the year. Cash balances are higher than expected due to recent new borrowing, offsetting the lower than forecast interest rates.

The Council's cash investments are held primarily for liquidity purposes and therefore only available for relatively short term deposits in a restricted selection of high quality instruments, which often generate sub-LIBOR/SONIA returns. In particular, a large proportion of cash funds at the report date were held with the UK Debt Management Office (part of HM Treasury) which is highly secure but only pays a low rate of interest (0.50%).

A full list of current investments is shown at Appendix 1.

Borrowing performance for 9 months ended 31 December 2019:

- 3.10 The Council requires external borrowing to fund its capital programme, and had total debt of £123m at the report date; 61% of the current debt is at fixed rate for the medium-long term from the Public Works Loan Board (PWLB), with the remainder short term variable rate from other local authorities. As borrowing will increase further, and the prospect of rate increases remains, we will closely monitor the interest rate situation, and may seek to take a higher proportion of the debt at medium-long term fixed rates. This may cost more in the short term but will provide certainty of cost and savings in the longer term.

It should be noted that the PWLB interest rates (which are linked to UK Gilt yields) were increased by an additional 1% across the board from 9 October 2019, making them relatively expensive and uncompetitive compared to other sources of funding

3.11 The table below shows the borrowing position as at 31 December 2019:

	Borrowing Amount £	Interest Rate	Interest Budget* £	Interest Actual^ £	Variance £
Apr-Dec 2019	£116.5m (average)	1.54% (annualised)	1,885k	1,345k	540k
As at 31/12/19	£123m	1.58%	-	-	-

* Original interest budget reduced by £250k

^ Interest payable relates to external loans only, excluding finance lease interest of £139k

Borrowing Benchmarking	3-year	5-year	10-year	20-year
Average PWLB Maturity rate Apr-Dec 2019	1.96%	1.96%	2.20%	2.69%

Interest payable for the full year is forecast to remain significantly under budget, due in part to lower interest rates than forecast, but also due to lower than expected loan drawdowns from Graven Hill, and cashflow updates on the CQ2 development.

A full list of current borrowing is shown at Appendix 1.

3.12 Non-treasury investment activity.

The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially to generate a profit.

As at 31 December 2019, the Council holds £64.3m of investments in the form of shares (£22.9m) and loans (£41.4m, excluding accrued interest) to subsidiary companies and other organisations, primarily Graven Hill and Crown House.

The loan elements of these non-treasury investments generate, or are expected to generate, a higher rate of return than earned on treasury investments, but this reflects the additional risks to the Council of holding such investments.

3.13 Overall performance

The overall performance for the 9 months to 31 December 2019 is as follows:

	Budget £k	Actual £k	Variance £k
Borrowing costs*	2,029	1,485	544
Treasury income	(115)	(172)	57
Non-treasury income	(2,252)	(3,079)	827
Total cost/(income)	(338)	(1,766)	1,428

*Borrowing costs include finance lease interest of £139k

The full year forecast is expected to achieve savings against budget of approximately £1.8m.

- 3.14 Our Treasury advisers, Arlingclose, provided the following economic commentary and interest rate forecast outlook. The report is dated 10 January 2020 so does not take into account the latest developments and events, particularly regarding coronavirus and its effects on the economy.

The global economy continues to slow on the back of ongoing geopolitical issues, primarily the trade policy stance of the US and its spat with China. However, it has been reported that Phase I of a trade deal between the two countries will be signed on 15th January 2020.

The UK economy continues to slow due to both post-Brexit uncertainty and the downturn in global activity. In response, global and UK interest rate expectations have eased. Central bank actions and geopolitical risks will continue to produce significant volatility in financial markets over the period, including bond markets.

Parliament passed Prime Minister Boris Johnson's Withdrawal Agreement Bill and the UK will now exit the EU on 31 January 2020. The bill also rules out an extension to the transition period for agreeing a trade deal which means a no-deal Brexit cannot be entirely ruled out for 2020.

Arlingclose expect the Bank Rate to remain at 0.75% for the foreseeable future but there remain substantial risks to this forecast, dependant on Brexit/trade deal outcomes as well as the evolution of the global economy. Arlingclose also expects gilt yields to remain at low levels for the foreseeable future and judges the risks to be weighted to the downside.

	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
Official Bank Rate													
Upside risk	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Arlingclose Central Case	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Downside risk	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75

4.0 Conclusion and Reasons for Recommendations

This report details the Treasury Performance for the Council for the period ending 31 December 2019.

5.0 Consultation

None

6.0 Alternative Options and Reasons for Rejection

The following alternative options have been identified and rejected for the reasons as set out below.

Option 1: To request further information on the performance reported.

7.0 Implications

Financial and Resource Implications

7.1 There are no financial implications arising directly from any outcome of this report.

Comments checked by: Dominic Oakeshott, Assistant Director - Finance (Interim)
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Legal Implications

7.2 There are no legal implications arising directly from any outcome of this report.

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Risk Management Implications

7.3 It is essential that this report is considered by the Audit Committee as it demonstrates that the risk of not complying with the Council's Treasury Management Policy has been avoided

Comments checked by: Louise Tustian, Head of Insight and Corporate Programmes
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8.0 Decision Information

Wards Affected

All wards are affected

Links to Corporate Plan and Policy Framework

Links to all areas of Corporate Plan

Lead Councillor

None

Document Information

Appendix No	Title
Appendix 1	CDC schedule of borrowing and investments at 31 December 2019 - EXEMPT
Background Papers	
None	
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