COTSWOLD
DISTRICT COUNCIL

Council Name	**COTSWOLD DISTRICT COUNCIL**
Name and date of Committee	**AUDIT COMMITTEE – 14 NOVEMBER 2019**
Report Number	**AGENDA ITEM 10**
Subject	**TREASURY MANAGEMENT MID-YEAR PERFORMANCE REPORT 2019-20**
Wards affected	ALL
Accountable member	Cllr Mike Evemy, Deputy Leader and Cabinet Member for Finance. Email: mike.evemy@cotswold.gov.uk
Accountable officer	Jenny Poole, Chief Finance Officer Tel: (01285) 623313 Email: jenny.poole@cotswold.gov.uk
Summary/Purpose	To receive and discuss the Council's Treasury Management performance for the period 1 April to 30 September 2019.
Annexes	None.
Recommendation	*That the Treasury Management mid-year performance be considered and recommended to Council for approval.*
Corporate priorities	
Key Decision	No
Exempt	No
Consultees/ Consultation	None

1. BACKGROUND

1.1 In February 2011 the Authority adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code). The Code requires Members of the Council to approve the treasury management strategy annually and receive a mid-year update on activity.

1.2 This report covers the treasury management activity and performance of Cotswold District Council for the period 1st April to 30th September 2019.

1.3 The Council's treasury management strategy for 2019/20 was approved at a meeting on 26th February 2019. The Council has 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 are therefore central to the council's treasury management strategy.

1.4 The 2017 Prudential Code includes a 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 authority's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 26th February 2019.

2. ECONOMIC UPDATE FOR THE PERIOD 1ST APRIL TO 30TH SEPTEMBER

2.1. UK Consumer Price Inflation (CPIH) fell to 1.7% year/year in August 2019 from 2.0% in July, weaker than the consensus forecast of 1.9% and below the Bank of England's target. The most recent labour market data for the three months to July 2019 showed the unemployment rate edged back down to 3.8% while the employment rate remained at 76.1%, the joint highest since records began in 1971. Nominal annual wage growth measured by the 3-month average excluding bonuses was 3.8% and 4.0% including bonuses. Adjusting for inflation, real wages were up 1.9% excluding bonuses (and 2.1% including).

2.2. The Quarterly National Accounts for Q2 GDP confirmed the UK economy contracted by 0.2% following the 0.5% gain in Q1 which was distorted by stockpiling ahead of Brexit. Only the services sector registered an increase in growth, a very modest 0.1%, with both production and construction falling and the former registering its largest drop since Q4 2012. Business investment fell by 0.4% (revised from -0.5% in the first estimate) as Brexit uncertainties impacted on business planning and decision-making.

2.3. Politics both home and abroad, continued to be a big driver of financial markets over the last quarter. Boris Johnson won the Conservative Party leadership contest and committed the Country to leaving the EU.

2.4. Tensions continued between the US and China with no trade agreement in sight and both countries imposing further tariffs on each other's goods. The US Federal Reserve cut its target Federal Funds rates by 0.25% in September to a range of 1.75% - 2%, a pre-emptive move to maintain economic growth amid escalating concerns over the trade war and a weaker economic environment leading to more pronounced global slowdown. The euro area Purchasing Manager Indices (PMIs) pointed to a deepening slowdown in the Eurozone. These elevated concerns have caused key government yield curves to invert, something seen by many commentators as a predictor of a global recession. Market expectations are for further interest rate cuts from the Fed and in September the European Central Bank reduced its deposit rate to -0.5% and announced the recommencement of quantitative easing from 1st November

2.5. The Bank of England maintained Bank Rate at 0.75% and in its August Inflation Report noted the deterioration in global activity and sentiment and confirmed that monetary policy decisions related to Brexit could be in either direction depending on when a deal is ultimately reached.

FINANCIAL MARKETS

2.6. After rallying early in 2019, financial markets have been adopting a more risk-off approach in the following period as equities saw greater volatility and bonds rallied (prices up, yields down) in a flight to quality and anticipation of more monetary stimulus from central banks. The Dow Jones, FTSE 100 and FTSE 250 are broadly back at the same levels seen in March/April.

2.7. Gilt yields remained volatile over the period on the back of ongoing economic and political uncertainty. From a yield of 0.63% at the end of June, the 5-year benchmark gilt yield fell to 0.32% by the end of September. There were falls in the 10-year and 20-year gilts over the same period, with the former dropping from 0.83% to 0.55% and the latter falling from 1.35% to 0.88%. 1-month, 3-month and 12-month LIBID (London Interbank Bid) rates averaged 0.65%, 0.75% and 1.00% respectively over the period.

2.8. Recent activity in the bond markets and PWLB interest rates highlight that weaker economic growth remains a global risk. The US yield curve remains inverted with 10-year Treasury yields lower than US 3-month bills. History has shown that a recession hasn't been far behind a yield curve inversion. Following the sale of 10-year Bunds at -0.24% in June, yields on German government securities continue to remain negative in the secondary market with 2 and 5-year securities currently both trading around -0.77%.

2.9. Credit Default Swap (CDS) spreads rose and then fell again during the quarter, continuing to remain low in historical terms. After rising to almost 120bps in May, the spread on non-ringfenced bank NatWest Markets plc fell back to around 80bps by the end of September, while for the ringfenced entity, National Westminster Bank plc, the spread remained around 40bps. The other main UK banks, as yet not separated into ringfenced and non-ringfenced from a CDS perspective, traded between 34 and 76bps at the end of the period.

2.10. There were minimal credit rating changes during the period. Moody's upgraded The Co-operative Bank's long-term rating to B3 and Fitch upgraded Clydesdale Bank and Virgin Money to A-.

3. TREASURY MANAGEMENT - SUMMARY POSITION 1/4/2019 TO 30/9/2019

3.1 On the 31st March 2019, the Council had net lending of £32.203m arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These factors are summarised in Table 1 below:

Table 1: Balance Sheet Summary

	31.3.19 Actual £m
General Fund – Capital Financing Requirement (CFR)	0
Less: External borrowing	0
Less: Usable reserves	(27.890)
Less: Working capital	(4.313)
Net lending	**(32.203)**

3.2 The Council's current strategy is to maintain investments below their underlying levels, known as internal borrowing, in order to reduce risk and keep interest costs low.

Table 2: Treasury Management Summary

	31.3.19 Balance £m	**Movement £m**	**30.9.19 Balance £m**	**30.9.19 Return %**
Long-term investments	12.301	0.199	12.500	4.06
Short-term investments	13.190	2.810	16.000	0.83
Cash and cash equivalents	6.712	(0.766)	5.946	0.73
Net Lending	**32.203**	**2.243**	**32.446**	**2.01**

3.3 At 30th September 2019 the Authority was debt free and has no immediate plans to borrow.

INVESTMENT PERFORMANCE AND PROJECTIONS

3.4 The Council holds invested funds, representing income balances and reserves. During the six month period the council's investment balance ranged between £26.4m and £42.00m due to timing differences between income and expenditure. The investment position, across investment type, as at the 30th September is shown below:

Table 3: Treasury Investment Position

	31.3.19 Balance £m	Net Movement £m	30.9.19 Balance £m	30.9.19 Return %
Banks & Building Societies (unsecured)	8.033	7.967	16.000	0.94
Local Authorities	5.010	(3.010)	2.000	1.00
Money Market Funds/ Call Accounts	6.712	(2.766)	3.946	0.73
Pooled Funds	12.448	0.052	12.500	4.64
Total Investments	**32.203**	**2.243**	**34.446**	**2.01**

3.5 Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking optimum rate of return, or yield. All investments made to date have been in line with the approved lending list, as set in February 2019.

3.6 In March 2019 the Council's Investment income for 2019/20 was budgeted to be £575,668. The average cash balances available for investment, representing the council's reserves and working balances, was £33.582m during the period this report covers.

3.7 Based upon current performance and returns the Council is on target to achieve in the region of £650,000 (at an average rate of return of 1.94%) for this financial year, generating a budget surplus in the region of £74,000.

POOLED FUNDS

3.8 Table 4 below shows the current valuations of the Pooled Funds portfolio at 30th September 2019, compared with the opening balances of 1st April 2019.

Table 4: Pooled Funds

FUND NAME	Initial Investment	1 April Fund Value	30th Sept Fund Value	Dividends in 2019/20 (as at 30 Sept)	Gain / (Loss) for 2019/20	Gain / (Loss) to Initial Principal
	£	£	£	£	£	£
CCLA Property Fund	500,000	511,537	506,759	11,168	(4,778)	6,759
CCLA Property Fund	2,000,000	1,872,848	1,855,357	40,889	(17,491)	(144,643)
Schroders Income Maximiser Fund	1,000,000	930,978	860,863	48,279	(70,115)	(139,137)
CCLA Diversified Income Fund	1,000,000	998,850	1,032,740	9,651	33,890	32,740
M&G UK Income Fund	2,000,000	1,932,672	1,948,542	62,622	15,870	(51,458)
Investec Diversified Fund	2,000,000	2,027,051	1,994,511	38,189	(32,540)	(5,489)
Columbia Threadneedle Bond Fund	2,000,000	2,026,591	2,075,104	30,577	48,513	75,104
Total	**10,500,000**	**10,300,527**	**10,273,876**	**241,375**	**(26,651)**	**(226,124)**

4. OUTLOOK FOR THE REMAINDER OF 2019/20

4.1 Having raised policy rates in August 2018 to 0.75%, the Bank of England's Monetary Policy Committee (MPC) has maintained expectations of a slow rise in interest rates over the forecast horizon.

4.2 The global economy is entering a period of slower growth in response to political issues, primarily the trade policy stance of the US. The UK economy has displayed a marked slowdown in growth due to both Brexit uncertainty and the downturn in global activity. In response, global and UK interest rate expectations have eased dramatically.

4.3 There appears no near-term resolution to the trade dispute between China and the US, a dispute that the US appears comfortable exacerbating further. With the 2020 presidential election a year away, Donald Trump is unlikely to change his stance.

4.4 The probability of a no-deal EU exit in the immediate term has decreased, although a no-deal Brexit cannot be entirely ruled out and the risk of this event remains for 2020. The upcoming general election may change the political landscape too.

4.5 The view is that the Bank Rate is to remain at 0.75% for the foreseeable future but there remain substantial risks to this forecast, dependant on Brexit outcomes and the evolution of the global economy. The Council's treasury advisors, Arlingclose, expect gilt yields to remain at low levels for the foreseeable future and judge the risks to be weighted to the downside and that volatility will continue to offer longer-term borrowing opportunities.

	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
Official Bank Rate													
Upside risk	0.00	0.00	0.25	0.25	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

5. COMPLIANCE

The Chief Finance Officer reports that all treasury management activities undertaken during the first six months complied fully with the CIPFA Code of Practice and the Authority's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated in table 6 below.

Table 6: Debt Limits

	30.9.19 Actual £m	2019/20 Operational Boundary £m	2019/20 Authorised Limit £m	Complied?
Borrowing	0.0	7.8	10.8	Yes
Total debt	**0.0**	**0.0**	**0.0**	