

TREASURY MANAGEMENT MID-YEAR REPORT 2018/19

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) which requires members to approve the treasury management semi-annual and annual reports.
- 1.2 The Council's treasury management strategy for 2018/19 was approved at a meeting on 20th February 2018. 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 is therefore central to the council's treasury management strategy.
- 1.3 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 but has yet to publish the local authority specific Guidance Notes to the latter. Also in England the Ministry for Housing Communities and Local Government (MHCLG) published its revised Investment Guidance which came into effect from April 2018.
- 1.4 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.

2. Economic update for the first six months

The following key points have been provided by the councils Treasury Advisors, Arlingclose.

- 2.1 Oil prices rose by 23% over the six months to around 82\$/barrel. UK Consumer Price Inflation (CPI) for August rose to 2.7% year on year, above the predicted forecast of the Bank of England's Inflation Report for August, as the effects of sterling's large depreciation in 2016 began to fade. The most recent labour market data for July 2018 showed the unemployment rate at 4% its lowest since 1975. The 3-month average annual growth rate for regular pay, i.e. excluding bonuses, was 2.9% providing some evidence that a shortage of workers is providing support to wages. However real wages, (adjusted for inflation), grew only by 0.2%, a marginal increase unlikely to have had much effect on households.
- 2.2 The Rebound in quarterly GDP growth in Q2 to 0.4% appeared to overturn the weakness in Q1 which was largely due to weather-related factors. However, the detail showed much of Q2 GDP growth was attributed to an increase in inventories. Year on year GDP growth at 1.2% also remains below trend. The Bank of England made no changes to monetary policy at its meetings in May and June, however hawkish minutes and a 6-3 vote to maintain rates was followed by a unanimous decision for a rate rise of 0.25% in August, taking Bank Rate to 0.75%.
- 2.3 Having raised rates in March, the US Federal Reserve again increased its target range of official interest rates in each of June and September by 0.25% to the current 2%-2.25%. Markets now expect one further rise in 2018. The escalating trade war between the US and China as tariffs announced by the Trump administration appeared to become an entrenched dispute, damaging not just China but also other Asian economies in the supply chain. The fallout, combined with tighter monetary policy, risks contributing to a slowdown in global economic activity and growth in 2019.
- 2.4 The EU Withdrawal Bill, which repeals the European Communities Act 1972 that took the UK into the EU and enables EU law to be transferred into UK law, narrowly made it through Parliament. With just six months to go when Article 50 expires on 29th March 2019, neither the Withdrawal Agreement between the UK and the EU which will be legally binding on separation issues and the financial settlement, nor its annex which will outline the shape of their future relationship, have been finalised, extending the period of economic uncertainty.

3. Treasury Management Summary Position 1/4/2018 to 30/9/2018

- 3.1 On 31st March 2018, the Council had net lending of £26.250m 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

	31.3.18 Actual £m
General Fund CFR	0
Internal borrowing	2.001
Less: Usable reserves	24.741
Less: Working capital	3.510
Net Investments	26.250

- 3.2 The Council's current strategy has been to maintain investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk and keep interest costs low. The treasury management position as at 30th September 2018 and the movement since April 2018 can be seen in Table 2 below.

Table 2: Treasury Management Summary

	31.3.18 Balance £m	Movement £m	30.9.18 Balance £m	30.9.18 Rate %
Long-term borrowing	0	0	0	
Short-term borrowing	2.000	(2.000)	0	
Total borrowing	2.000	(2.000)	0	
Long-term investments	4.570	5.930	10.500	4.28
Short-term investments	21.000	(8.000)	13.000	0.75
Cash and cash equivalents	2.680	8.290	10.970	0.51
Total investments	28.250	6.220	34.470	1.16
Net Lending	26.250	8.290	34.470	

4. Investments

- 4.1 The Council holds significant invested funds, representing income received in advance of expenditure plus balances, reserves held and money borrowed in advance of need. During the six month period the council's investment balance ranged between £24.765m and £40.525m due to timing differences between income and expenditure. The investment position is shown in Table 3 below.

Table 3: Treasury Investment Position

	31.3.18 Balance £m	Net Movement £m	30.9.18 Balance £m	30.9.18 Rate of Return%
Fixed Term Deposits – (Unsecured)	25.000	(8.000)	17.000	0.77
Money Market Funds/ Call Accounts	2.680	8.290	10.970	0.54
CCLA Property Fund	0.500	2.000	2.500	3.80
Schroders Maximiser Fund	-	1.000	1.000	6.80
M&G UK Equity Income Fund	-	2.000	2.000	3.00
CCLA Diversified Income Fund	-	1.000	1.000	4.97
Total Investments	28.180	6.290	34.470	1.16

- 4.2 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 in this financial year have been in line with the approved lending list set in February 2018.
- 4.3 In February 2018 the Council's Investment income for 2018/19 was budgeted to be £341,270. The average cash balances representing the council's reserves and working balances, was £36.643m during the period this report covers. The Council anticipates an investment outturn of £425,800 at a rate of return of 1.16% for this financial year. Estimated surplus for investment income is to be £84.530k for the financial year.
- 4.4 In the first part of the financial year a decision to invest further funds in the CCLA Property Fund and new investments with Schroders Income Maximiser Fund, CCLA Diversified Income Fund and the M&G UK Equity Fund haven proven successful so far with returns being higher than expected. Further new Funds are being looked at which will hopefully see higher returns when reported in the annual outturn report. Please see Table 4 below showing the latest values and any dividends received to date.

Table 4: Pooled Funds Summary

	Initial Investment	31 Sept 2018 Fund Value	Dividends paid out in 2018/19 as at 30 Sept	Gain / (Loss) for 2018/19	Gain / (Loss) to Initial Principal
	£	£	£	£	£
CCLA Property Fund	2,500,000	2,360,852	19,341	*(139,148)	*(139,148)
Schroders Inc Max Fund	1,000,000	1,003,178	-	3,178	3,178
M&G Income Dist Fund	2,000,000	1,955,338	-	(44,662)	(44,662)
CCLA Diversified Fund	1,000,000	1,003,178	-	3,178	3,178
September 2018 Total	6,500,000	6,322,546	19,341	(177,454)	(177,454)

* This reflects the fees paid up front for the £2m invested in April 2018

5. Outlook for the Remainder of 2018/19

- 5.1 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.

- 5.2 The MPC has a definite bias towards tighter monetary policy but is reluctant to push interest rate expectations too strongly. While policymakers are wary of domestic inflationary pressures over the next two years, it is believed that the MPC members consider both that (a) ultra-low interest rates result in other economic problems, and that (b) higher Bank Rate will be a more effective weapon should the downside Brexit risks crystallise and cuts are required.
- 5.3 Arlingclose's central case is for Bank Rate to rise twice in 2019. The risks are weighted to the downside.

	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21
Official Bank Rate													
Upside risk	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Arlingclose Central Ca:	0.75	0.75	1.00	1.00	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25
Downside risk	0.00	0.00	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75

6. Compliance

- 6.1 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 5 below.

Table 5: Debt Limits

	30.9.18 Actual £m	2018/19 Operational Boundary	2018/19 Authorised Limit	Complied? Yes/No
Borrowing	-	4.50	6.5	Yes
Total debt	-	4.5	6.5	

- 6.2 Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

7. Principal Sums Invested for Periods Longer than 365 days

The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long term principal sum invested to final maturities beyond the period end were:

	2017/18 Actuals	2018/19
Actual principal invested beyond one year	£2m	£8.5m
Limit on principal invested beyond one year	£10m	£20.0m
Complied	Yes	Yes

(END)