# AGENDA ITEM NO 8

**REPORT NO 422/17**

**ANGUS COUNCIL**

**ANGUS COUNCIL - 7 DECEMBER 2017**

**TREASURY MANAGEMENT 2017/18 MID-YEAR REVIEW REPORT**

**REPORT BY HEAD OF CORPORATE FINANCE**


**ABSTRACT**

Members are asked to scrutinise Angus Council's mid-year review report on treasury management activities for the period 1 April 2017 to 30 September 2017.


## 1 RECOMMENDATIONS

1.1 It is recommended that the Council:

i. Scrutinise the Angus Council mid-year review report on treasury management activities for the period 1 April 2017 to 30 September 2017 attached at Appendix 1;

## 2 ALIGNMENT TO THE ANGUS COMMUNITY PLAN / SINGLE OUTCOME AGREEMENT / COPORATE PLAN

2.1 Effective Treasury Management maximises the resources available to the Council to provide services. The activities undertaken through the Council's treasury management processes (as reflected in **Appendix 1** to this report) therefore contribute as a whole to the local outcomes contained within the Angus Community Plan and Single Outcome Agreement 2013-2016.

## 3 BACKGROUND

3.1 The need to prepare a treasury management mid-year review report is a minimum requirement of the Treasury Management in the Public Services Code of Practice published by the Chartered Institute of Public Finance and Accountancy, the latest version of which was issued in 2011.

3.2 Members should note Report 244/10 to Angus Council dated 25 March 2010 at which the Code of Practice was adopted for implementation on 1 April 2010 within the Council. The Code requires that Members be kept informed of treasury management activities at least twice a year in the form of an annual report after each financial year and a mid-year review report halfway through each financial year. This report therefore ensures compliance with the Code of Practice.

## 4 TREASURY MANAGEMENT 2017/18 MID-YEAR REVIEW REPORT

4.1 The treasury management mid-year review report details Angus Council's treasury management activities for the period 1 April 2017 to 30 September 2017 and is attached at Appendix 1 for consideration by Members.

## 5 MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE 2

5.1 Members attention is drawn to a financial markets regulatory change which takes effect from 3 January 2018 and which is being brought about by the implementation of a piece of European legislation called the Markets in Financial Instruments Directive 2 – more commonly referred to as "MiFID 2".

5.2 This legislation is designed to offer greater protection for investors and bring more transparency to all investment classes, including those utilised by the Council. The Directive categorises investors as either "Retail" or "Professional" – with the key difference being the range of financial products that can be accessed by each investor category. The Directive initially categorises Councils as "Retail" investors – which limits the range of products available – but with the option for Councils to choose (or "opt up") to be categorised as "Professional" investors, thus opening up access to the full range of investment products.

5.3 For the Council's purpose, we currently use some investment products accessible only at the "Professional" investor level due to the comparatively advantageous interest rates available. This currently only affects investments that the Council makes in financial products which can effectively be traded – largely these are Certificates of Deposit and Money Market Funds.

5.4 Members are asked to note that to ensure that the Council continues to have access to the full range of financial products – and therefore full flexibility in managing the Council's cash flows – the Head of Corporate Finance has taken the necessary actions to "opt up" to "Professional" status such that this is in place for 3 January 2018 Directive implementation date.

## 6 RISK IMPLICATIONS

6.1 This report does not require any specific risk issues to be addressed, however members will be aware that the management of risk is an integral part of the Council's treasury management activities.

## 7 FINANCIAL IMPLICATIONS

7.1 There are no direct financial implications arising from the recommendations in this report. An effective treasury management service does however form a significant part of the Council's financial arrangements and its financial wellbeing.

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NOTE

No background papers as defined by Section 50D of the Local Government (Scotland) Act 1973 (other than any containing confidential or exempt information) were relied on to any material extent in preparing this Report.

List of Appendices

Appendix 1: Angus Council - Treasury management mid-year review report for the period 1 April 2017 to 30 September 2017

**Appendix 1**

**Angus Council - Treasury management mid-year review report for the period 1 April 2017 to 30 September 2017**

The mid-year review report has been prepared in compliance with the Chartered Institute of Public Finance and Accountancy's Treasury Management Code of Practice and covers the following:

- borrowing position at 30 September 2017;
- capital financing requirement
- long term borrowing undertaken in the first six months of 2017/18;
- long term borrowing repaid in the first six months of 2017/18;
- PWLB interest rates forecast;
- investment position at 30 September 2017;
- debt rescheduling;
- variations from agreed policies and practices;
- compliance with treasury and prudential limits;

Members may recall the Treasury Management Annual Report 2016/17 (Report 356/17 refers) which noted that the loans pool interest rate for all Scottish Local Authorities was not available at that time. Members may wish to note however that on the basis of year end returns from individual councils, a 2016/17 loans pool rate for Scottish Local Authorities has now been calculated and averages 4.13%. Members are reminded that Angus Council's audited loans pool interest rate for the financial year 2016/17 was 4.44%.

Members should note however that the Average Loans Pool Rate as a comparative is not overly relevant as each Local Authority adopts its own bespoke treasury strategy.

1. **<u>Borrowing position at 30 September 2017</u>**

The Council's gross and net external debt positions as at 30 September 2017 are shown in Table 1 below. The gross and net external debt positions as at 1 April 2017 are also shown for comparative purposes.

**Table 1**

| External Debt | Total Principal as at 30 September 2017 | Total Principal as at 1 April 2017 |
|---|---|---|
| Fixed Rate Borrowing – P W L B * | £124.739 million | £128.739 million |
| Fixed Rate Borrowing – LOBO ** | £16.000 million | £30.000 million |
| Fixed Rate Borrowing – Market *** | £14.000 million | £00.000 million |
| **Total External Debt** | **£154.739 million** | **£158.739 million** |
| Investments | (£56.308 million) | (£46.845 million) |
| Total Net External Debt | £98.431 million | £111.894 million |

**<u>Notes</u>**

* PWLB = Public Works Loans Board
** LOBO borrowing is from banks and similar financial institutions – These loans allow the lender to vary the rate of interest at specific points in time (referred to as call dates) but the Council is not legally obliged to accept such changes hence both the lender and borrower have options on whether to continue the loan or not.
*** Market borrowing is from banks and similar institutions in traditional fixed rate and fixed term form. This debt was previously shown under the LOBO category and was contained in the £30 million value shown in table 1 above for 1 April 2017. During 2017/18 however, the 3 loans which comprise this market debt were converted by the lender from LOBOs to straightforward fixed term and fixed rate loans and are therefore no longer categorised as LOBO debt.

1.1 <u>Capital Financing Requirement</u>

The Council calculates a rolling 12 month forecast of its Capital Financing Requirement (C F R). The C F R represents the level of borrowing for capital purposes which it is projected that the

Council requires to have in place, including the gross external debt already in place, at the end of the rolling 12 month period. The forecast C F R at any point in time therefore essentially takes the existing gross external debt and adjusts for projected net capital expenditure over the forthcoming 12 month period. The C F R therefore denotes a snapshot of the underlying need to borrow for capital purposes and this makes it a crucial part of our borrowing arrangements in compliance with relevant Codes of Practice. At 30 September 2017 the C F R was projected to be £182.312 million (that is to say the projected value of our external debt requirements at 30 September 2017).

Where there is headroom between existing gross external debt levels and the C F R, the Council may, at any time over the 12 month period, borrow from the Public Works Loan Board (P W L B) or the money market (external borrowing). Alternatively the Council may on a temporary basis borrow from internal balances (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. When the gross external debt and C F R information shown above is taken into account, it can be seen that there is borrowing headroom at 30 September 2017 of £25.573 million (C F R of £182.312 million less Gross Debt of £154.739 million). This is however a snapshot position and members are asked to note that the headroom is projected to rise over the remainder of the financial year.

1.2 <u>Long term borrowing undertaken in the first six months of 2017/18</u>

Members are asked to note that no new borrowing has been undertaken during the period 1 April 2017 to 30 September 2017. Whilst there is an underlying need to borrow for capital purposes, the council currently holds significant levels of temporary cash in balances therefore new long term borrowing has been deferred over the first half of the year, with the intention of reducing underlying cash balances. This deferment strategy benefits the council by reducing the total interest payable on Debt.

The latest interest rate forecast provided by the Council's Treasury Management advisers (detailed in Table 4 below) indicates that P W L B interest rates for new borrowing are projected to rise steadily over the next 2 years.

In respect of potential borrowing from the P W L B, the Council has access to a 20 basis point (0.20%) discount (otherwise known as the certainty rate) on all borrowing undertaken from the Public Works Loan Board in return for providing information on potential long term borrowing and associated capital spending plans. Angus Council will continue to annually submit the information necessary to ensure ongoing access to the reduced borrowing rates.

Having taken account of:

- the interest rate forecast (Table 4 below);
- the certainty rate discount on new borrowing detailed above;
- external advice from the Council's treasury advisers;
- the current and projected headroom between the Council's current external debt and the C F R; and
- the current and projected levels of cash balances,

it is the view of the Head of Corporate Finance that significant amounts of new borrowing are unlikely to be undertaken this financial year.

Although the Council has a significant capital programme it is currently more appropriate to use surplus cash balances held to finance that capital expenditure before considering taking out new loans. This approach makes sense both in terms of managing counterparty risk and also allows the Council to postpone the cost of new borrowing.

Further borrowing could still however be undertaken should prevailing economic and market conditions over the remainder of the financial year move to the advantage of the Council. It is also possible that non - P W L B borrowing may become more competitive compared with P W L B rates and the Head of Corporate Finance will closely monitor the situation to ensure that any appropriate borrowing opportunities are fully considered and actioned where this is of benefit to the Council.

As previously, it would be intended that any such borrowing will be taken at a number of points during the year to mitigate the risk of interest rate movements and taking cognisance of the subsequent lending opportunities that are available in respect of the net cost of incurring additional borrowing.

In accordance with the 2017/18 Treasury Management Strategy Statement, the Council has not borrowed in advance of need during the first half of the 2017/18 financial year and has no intention to borrow in advance for the remainder of the 2017/18 financial year.

1.3 Long term borrowing repaid in the first six months of 2017/18

The Council has repaid £4.000million of P W L B loans that naturally matured in the period 1 April 2017 to 30 September 2017. Details of the loans repaid are shown in Table 2 below.

**Table 2**

| Date Repaid | Amount (£) | Rate (%) |
|---|---|---|
| 30/05/2017 | 4,000,000 | 3.42 |
| **Totals** | **4,000,000** | 3.42 |

A further £741,000 of P W L B matures during the second half of the financial year.

1.4 P W L B interest rates

The highest and lowest P W L B interest rates available during the period 1 April 2017 to 30 September 2017 for 5, 10, 25 and 50 year terms are detailed in Table 3 below. For clarity the rates shown within Table 3 have been reduced to reflect the 20 basis point P W L B certainty rate discount. It will be noted that even in a short period of only six months there has been sizeable movements in the rates available.

**Table 3**

| Period | Interest Rate Low Point (%) | Interest Rate High Point (%) |
|---|---|---|
| 5 years | 1.08 | 1.62 |
| 10 years | 1.81 | 2.22 |
| 25 years | 2.54 | 2.83 |
| 50 years | 2.26 | 2.57 |

The Capita Treasury Services revised forecast for U K Bank Base Rate and new P W L B borrowing interest rates issued on 7th November 2017 is as follows:

**Table 4**

| Rate | Dec 17 | Mar 18 | Jun 18 | Sep 18 | Dec 18 | Mar 19 | Jun 19 | Sep 19 |
|---|---|---|---|---|---|---|---|---|
| **Base Rate** | 0.50% | 0.50% | 0.50% | 0.50% | 0.75% | 0.75% | 0.75% | 0.75% |
| **5 Year** | 1.50% | 1.60% | 1.60% | 1.70% | 1.80% | 1.80% | 1.90% | 1.90% |
| **10 Year** | 2.10% | 2.20% | 2.30% | 2.40% | 2.40% | 2.50% | 2.60% | 2.60% |
| **25 Year** | 2.80% | 2.90% | 3.00% | 3.00% | 3.10% | 3.10% | 3.20% | 3.20% |
| **50 Year** | 2.50% | 2.60% | 2.70% | 2.80% | 2.90% | 2.90% | 3.00% | 3.00% |

The above forecasts for P W L B rates have been reduced to reflect the P W L B certainty rate discount as highlighted above in Section 1.2 of this appendix.

2. **Investment position at 30 September 2017**

In accordance with the Chartered Institute of Public Finance and Accountancy's Code of Practice, it is the Council's investment priority to: ensure the security of capital; ensure availability of liquidity; and thereafter to obtain an appropriate level of return which is consistent with the Council's risk appetite.

The average daily level of funds available for investment purposes in the first six months of 2017/18 was £55.960million. These funds were available on a temporary basis, and the level of funds that were available was mainly dependent on the timing of payments, receipt of grants and progress on the capital programme.

The counterparty limits approved within the Annual Investment Strategy were not breached during the first six months of 2017/18.

Notwithstanding the historically low Bank of England base rate and the Council's cautious and controlled approach to lending, a rate of return for the period 1 April 2017 to 30 September 2017 was achieved, as follows:

**Table 5**

| Average Daily Investment Exposure £m | Angus Council Rate of Return (%) | 6 Month Benchmark Return (%) | Internally set local investment rate target (%) |
|---|---|---|---|
| 55.960 | 0.53 | 0.40 | 0.50 |

The benchmark included above represents the 6 month London Interbank Bid rate. It can be seen from the above table that the Angus Council rate of return is 0.13% higher than the above benchmark and 0.03% higher than the internally set local investment rate target of 0.50% as set out in the annual strategy.

3. **Debt rescheduling**

No debt rescheduling was undertaken during the first six months of 2017/18 as the opportunity to reschedule debt has been limited in the current economic climate. This situation is expected to continue for the foreseeable future, however when interest rates begin to rise again there may be opportunities for debt rescheduling.

4. **Variations from agreed policies and practices**

The Treasury Management Strategy Statement for 2017/18 was approved by the Council on 23 March 2017 (Report 109/17 refers). No adjustments to the strategy were made when the Treasury Management Annual Report was presented to Angus Council on 19 October 2017 (Report 35617 refers) and the Head of Corporate Finance is not recommending any changes at this time.

There were also no variations from agreed policies or practices to report during the period 1 April 2017 to 30 September 2017.

5. **Compliance with Treasury and Prudential Limits**

It is a statutory duty for the Council to determine and keep under review "Affordable Borrowing Limits". The Council's approved Prudential Indicators are outlined in the 2017/18 Treasury Management Strategy Statement and detailed in the Setting of Prudential Indicators for 2017/18 Budget Process Committee Report (report number 63/17 to the Special Budget Meeting of Angus Council on 16 February 2017).

During the first six months of the 2017/18 financial year the Council has operated within the treasury limits and Prudential Indicators set out in the Council's 2017/18 Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices.