**AGENDA ITEM NO 10**
**REPORT NO 406/19**

**ANGUS COUNCIL**

**5 DECEMBER 2019**

# TREASURY MANAGEMENT 2019/20 MID-YEAR REVIEW

**REPORT BY DIRECTOR OF FINANCE**


**ABSTRACT**
Members are asked to scrutinise Angus Council's mid-year review of treasury management activities for the period 1 April 2019 to 30 September 2019.


## 1 RECOMMENDATION

1.1 It is recommended that the Council scrutinise the Angus Council mid-year review of treasury management activities for the period 1 April 2019 to 30 September 2019, as attached at **Appendix 1**.

## 2 ALIGNMENT TO THE COUNCIL PLAN / LOCAL OUTCOMES IMPROVEMENT PLAN

2.1 Treasury management is the management of borrowing, investments and cash flows; banking, money market and capital market transactions; the effective control of risks associated with those activities; and the pursuit of optimum performance consistent with those risks. Effective treasury management therefore maximises the resources available to the Council to provide services.

2.2 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 outcomes contained within the Council Plan and Local Outcome Improvement Plan.

## 3 BACKGROUND

3.1 The annual minimum reporting requirements with regard to treasury management (per the Treasury Management in the Public Services Code of Practice (2017 edition) and the Prudential Code for Capital Finance in Local Authorities (2017 edition), both published by the Chartered Institute of Public Finance and Accountancy (CIPFA)) are that full Council should receive the following reports:

- an annual treasury strategy in advance of the year (for 2019/20, report 74/19 refers)
- a mid-year treasury management review (this report)
- an annual report following the year end describing the activity compared to the strategy (this will be produced after the 2019/20 year end).

3.2 This treasury management mid-year review details Angus Council's treasury management activities for the period 1 April 2019 to 30 September 2019 (as attached at **Appendix 1**), thereby ensuring compliance with the aforementioned CIPFA Codes of Practice.

## 4 INCREASE IN THE COST OF BORROWING FROM THE PWLB

4.1 On 9 October 2019, HM Treasury unexpectedly announced an increase to the interest rate for Public Works Loans Board (PWLB) loans by one percentage point with immediate effect. PWLB lending is offered at a fixed margin above the Government's cost of borrowing, as measured by gilt yields. That fixed margin is now gilt plus 200 basis points for lending at the Standard Rate (increased from gilt plus 100 basis points) and gilt plus 180 basis points for lending at the Certainty Rate (increased from gilt plus 80 basis points). This means that for each £1.0m borrowed, these higher rates increase the annual interest payable by circa £10,000.

4.2 It should be noted Angus Council has access to the Certainty Rate on all borrowing undertaken from the PWLB in return for providing information on potential long term borrowing and associated capital spending plans.

4.3 The PWLB is the main source of finance for the majority of the UK's local authority capital investment programmes, including that of Angus Council. It is believed that the increase has been brought about in an effort to manage the levels of borrowing that have been incurred by English local authorities in particular over recent years, largely for commercial purposes. PWLB also have borrowing limits set by HM Treasury which they need to comply with and the risk to this has been cited as part of the reason for the increase in rates.

4.4 The interest rate increase will impact on new rather than existing loans. Continuing high levels of temporary surplus cash balances has meant Angus Council has not actually borrowed from the PWLB since August 2016 and had not anticipated borrowing certainly for the remainder of this financial year. Members are reminded that as a matter of policy the Council will not borrow more than, or in advance of, its needs purely in order to profit from the investment of the extra sums borrowed as such action is illegal (as noted in the approved annual Treasury Management Strategy Statement).

## 5 REVIEW OF ANGUS COUNCIL LOANS FUND

5.1 The Local Authority (Capital Financing and Accounting) (Scotland) Regulations 2016 sets out the statutory arrangements for local authority borrowing and lending and the requirement to maintain a loans fund. The 2016 Regulations replace the statutory arrangements set out in the Local Government (Scotland) Act 1975 (Schedule 3).

5.2 The loans fund essentially acts as an internal bank for the council, providing the long term financing (known as loans fund advances) that it needs for capital investment. Angus Council's treasury advisors, Link Asset Services, are currently undertaking a review of the loans fund as a result of revised flexibility that the 2016 Regulations has granted to local authorities on how they account for loans fund advances. On the basis of this flexibility, a saving to the corporate loan charges budget (which meets the costs associated with loans fund advances – repayment of principal, interest and expenses) of £1m has been included within the Change Programme in 2020/21. Upon conclusion of Link's review, any consequential changes to accounting policies will be brought before the relevant committee for approval. It is intended that further member training on treasury management will be organised to coincide with the proposed changes to loans fund advances.

## 6 RISK IMPLICATIONS

5.1 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.

**REPORT AUTHOR:** **Dawn Johnston**
**EMAIL DETAILS:** **Finance@angus.gov.uk**

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 for the period 1 April 2019 to 30 September 2019

**Appendix 1**

**Treasury Management Mid-Year Review for the Period 1 April 2019 to 30 September 2019**

## 1. Introduction

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

- borrowing position at 30 September 2019 (section 2)
- capital financing requirement (section 3)
- long term borrowing undertaken (section 4)
- long term borrowing repaid (section 5)
- PWLB interest rates (section 6)
- investment position at 30 September 2019 (section 7)
- debt rescheduling
- variations from agreed policies and practices
- compliance with treasury and prudential limits.

1.2 The 2019/20 Treasury Management Strategy Statement (TMSS) was approved by this council on 21 March 2019 (report 74/19 refers). There are no policy amendments required to the TMSS based on the latest economic position or budgetary changes already approved.

## 2. Borrowing Position at 30 September 2019

2.1 The Council's gross and net external debt positions as at 30 September 2019 are shown in Table 1 below. The gross and net external debt positions as at 1 April 2019 are also shown for comparative purposes.

**Table 1**

| External Debt | Position as at 30 September 2019 £m | Position as at 1 April 2019 £m |
|---|---|---|
| Fixed Rate Borrowing – PWLB * | 114.867 | 117.756 |
| Fixed Rate Borrowing – LOBO ** | 16.000 | 16.000 |
| Fixed Rate Borrowing – Market *** | 14.000 | 14.000 |
| **Total External Debt** | **144.867** | **147.756** |
| Investments | (74.408) | (61.859) |
| Total Net External Debt | 70.459 | 85.897 |

**Notes**

* 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.

## 3. Capital Financing Requirement

3.1 The Council calculates a rolling 12 month forecast of its Capital Financing Requirement (CFR). The CFR 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 CFR 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 CFR 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 2019 the CFR was projected to be £175.094 million (that is to say the projected value of our external debt requirements at 30 September 2019).

3.2 Where there is headroom between existing gross external debt levels and the CFR, the Council may, at any time over the 12 month period, borrow from the Public Works Loan Board (PWLB) 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 CFR information shown above is taken into account, it can be seen that there is borrowing headroom at 30 September 2019 of £30.762 million (CFR of £175.094 million less gross debt of £144.867 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.

## 4. Long Term Borrowing Undertaken

4.1 Members are asked to note that no new borrowing has been undertaken during the period 1 April 2019 to 30 September 2019. Whilst there is an underlying need to borrow for capital purposes, as the council currently holds significant levels of temporary cash in balances 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 providing interest rates do not rise significantly in the interim.

4.2 The latest interest rate forecast provided by the Council's treasury management advisers (detailed in Table 4 below) indicates that PWLB interest rates for new borrowing are projected to rise steadily but gradually over the next 2 years.

4.3 In respect of potential borrowing from the PWLB, the Council has access to a 20 basis point (0.20%) discount (otherwise known as the Certainty Rate) on all borrowing undertaken from PWLB 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.

4.4 It is the view of the Director of Finance that significant amounts of new borrowing are unlikely to be undertaken over the remainder of the financial year, 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 CFR; and
- the current and projected levels of cash balances.

4.5 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.

4.6 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-PWLB borrowing may become more competitive compared with PWLB rates and the Director of 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.

4.7 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.

4.8 In accordance with the 2019/20 Treasury Management Strategy Statement, the Council has not borrowed in advance of need during the first half of the 2019/20 financial year and has no intention to borrow in advance for the remainder of the 2019/20 financial year.

## 5. Long Term Borrowing Repaid

5.1 The Council has repaid £2.889 million of PWLB loans that naturally matured in the period 1 April 2019 to 30 September 2019, the details of which are shown in Table 2 below:

**Table 2**

| Date Repaid | Amount £m | Rate % |
|---|---|---|
| 15/05/19 | 0.445 | 9.375 |
| 16/08/19 | 2.000 | 3.240 |
| 30/09/19 | 0.445 | 9.375 |
| **Totals** | **2.889** | |

5.2 A further £296,441 of PWLB (at an interest rate of 9.625%) matures during the second half of the financial year.

## 6. PWLB Interest Rates

6.1 The lowest, highest and average PWLB interest rates available during the period 1 April 2019 to 30 September 2019 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 PWLB 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 % | Average Interest Rate % |
|---|---|---|---|
| 5 years | 1.01 | 1.73 | 1.37 |
| 10 years | 1.13 | 2.07 | 1.62 |
| 25 years | 1.73 | 2.58 | 2.20 |
| 50 years | 1.57 | 2.41 | 2.07 |

6.2 The council's treasury advisor, Link Asset Services, has provided the following forecast for UK Bank Rates (also known as the Base Rate) and new PWLB borrowing interest rates (again reflecting the Certainty Rate discount), as detailed in Table 4 below.

**Table 4**

| Rate | Dec 19 % | Mar 20 % | Jun 20 % | Sep 20 % | Dec 20 % | Mar 21 % | Jun 21 % | Sep 21 % |
|---|---|---|---|---|---|---|---|---|
| Bank Rate | 0.75 | 0.75 | 0.75 | 0.75 | 1.00 | 1.00 | 1.00 | 1.00 |
| 5 Year | 2.30 | 2.50 | 2.60 | 2.70 | 2.70 | 2.80 | 2.90 | 3.00 |
| 10 Year | 2.60 | 2.80 | 2.90 | 3.00 | 3.00 | 3.10 | 3.20 | 3.30 |
| 25 Year | 3.30 | 3.40 | 3.50 | 3.60 | 3.70 | 3.70 | 3.80 | 3.90 |
| 50 Year | 3.20 | 3.30 | 3.40 | 3.50 | 3.60 | 3.60 | 3.70 | 3.80 |

## 7. Investment Position at 30 September 2019

7.1 In accordance with CIPFA's Treasury Management Code of Practice, it is the council's investment priority to:

- ensure the **security** of capital (i.e. the safety of the investment);
- ensure the availability of **liquidity** (i.e. the accessibility of the cash); and
- thereafter to obtain an appropriate level of **return** (i.e. the income received) which is consistent with the council's risk appetite.

7.2 The average daily level of funds available for investment purposes in the first six months of 2019/20 was £73.238 million. 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 other income and progress on the capital programme.

7.3 The counterparty limits approved within the Annual Investment Strategy were not breached during the first six months of 2019/20.

7.4 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 2019 to 30 September 2019 was achieved, as follows:

**Table 5**

| Average Daily Investment Exposure £m | Angus Council Rate of Return % | 6 Month Benchmark Return % | Internally Set Investment Rate Target % |
|---|---|---|---|
| 73.238 | 0.96 | 0.70 | 0.95 |

7.5 The benchmark included above represents the 6 month London Interbank Bid (LIBID) rate as at 30 September 2019. It can be seen from the above table that the Angus Council rate of return is 0.26% higher than the LIBID benchmark and 0.01% higher than the internally set local investment rate target of 0.95% as set out in the annual strategy.

## 8. Debt Rescheduling

8.1 No debt rescheduling was undertaken during the first six months of 2019/20 as the opportunity to reschedule debt has been limited in the current economic climate. This situation is expected to continue for the foreseeable future.

## 9. Variations from Agreed Policies and Practices

9.1 The Treasury Management Strategy Statement for 2019/20 was approved by Angus Council on 21 March 2019 (report 74/19 refers). No adjustments to the strategy were made when the Treasury Management Annual Report for 2018/19 was presented to Angus Council on 17 October 2019 (report 314/19 refers) and the Director of Finance is not recommending any changes at this time.

9.2 There were also no variations from agreed policies or practices to report during the period 1 April 2019 to 30 September 2019.

## 10. Compliance with Treasury and Prudential Limits

10.1 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 2019/20 Treasury Management Strategy Statement and detailed in the Setting of Prudential Indicators for 2019/20 Budget Process committee report (report number 63/19 to the Special Budget Meeting of Angus Council on 21 February 2019).

10.2 During the first six months of the 2019/20 financial year the Council has operated within the treasury limits and Prudential Indicators set out in the Council's 2019/20 Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices.