0REPORT REFERENCE NO.	**RC/19/8**
MEETING	**RESOURCES COMMITTEE**
DATE OF MEETING	**15 MAY 2019**
SUBJECT OF REPORT	**TREASURY MANAGEMENT – QUARTER FOUR AND ANNUAL REPORT 2018-19**
LEAD OFFICER	**Director of Finance (Treasurer)**
RECOMMENDATIONS	***That the performance in relation to the treasury management activities of the Authority for 2018-19 including the fourth quarter, as set out in this report, be noted.***
EXECUTIVE SUMMARY	The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management, requires that the Authority receives a report in respect of borrowing and investment activities during the year, and compares this performance against the treasury management strategy adopted. The report includes a performance report relating to the final quarter of the 2018-19 financial year and a summary of annual performance. A representative (Adam Burleton) from Link Asset Services, the Authority external treasury management advisors, will be in attendance at the meeting to present the performance report.
RESOURCE IMPLICATIONS	As indicated within the report.
EQUALITY RISK AND BENEFIT ASSESSMENT (ERBA)	An initial assessment has not identified any equality issues emanating from this report.
APPENDICES	A. Prudential indicators 2018-19 B. Glossary of Terms
LIST OF BACKGROUND PAPERS	Treasury Management Strategy (including Prudential and Treasury Indicators) Report to budget meeting held on the 16th February 2018 – Minute DSFRA/64c refers

1. INTRODUCTION

1.1. The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management recommends that members be updated on treasury management activities regularly (annual, mid-year or quarterly reports). The Authority fully complies with the primary requirements of the Code, which includes:

- The creation and maintenance of a Treasury Management Policy Statement, which sets out the policies and objectives of the Authority's treasury management activities.
- The creation and maintenance of Treasury Management Practices, which set out the manner in which the Authority will seek to achieve those policies and objectives.
- The receipt by the Authority of an annual strategy report for the year ahead, a mid-year treasury update report and an annual review report of the previous year.
- The delegation by the Authority of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
- Delegation by the Authority of the role of scrutiny of treasury management strategy and policies to a specific named body which in this Authority is the Resources Committee.
- Minimum reporting requirements, in addition, the Resources Committee has received quarterly treasury management update reports.

1.2. The regulatory environment places responsibility on Members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Authority's policies previously approved by Members.

1.3. The Authority confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Resources Committee before they were reported to the full Authority. Members have been supported in their scrutiny role through regular updates and the attendance at Committee meetings by the Authority's Treasury Management advisors, Link Asset Services.

1.4. A glossary of terms and acronyms used is provided at Appendix B of this report

2. THE ECONOMY AND INTEREST RATES

UK

2.1. After weak economic growth of only 0.1% in quarter one of 2018/19, growth picked up to 0.4% in quarter 2 and to a particularly strong 0.7% in quarter 3, before cooling off to 0.2% in the final quarter. Given all the uncertainties over Brexit, this weak growth in the final quarter was as to be expected. However, some recovery in the rate of growth is expected going forward. The annual growth in Q4 came in at 1.4% y/y confirming that the UK was the third fastest growing individual country in the G7 in quarter 4.

2.2. After the Monetary Policy Committee raised Bank Rate from 0.5% to 0.75% in August 2018, it is little surprise that they have abstained from any further increases since then. We are unlikely to see any further action from the MPC until the uncertainties over Brexit clear. If there were a disorderly exit, it is likely that Bank Rate would be cut to support growth. Nevertheless, the MPC does have concerns over the trend in wage inflation which peaked at a new post financial crisis high of 3.5%, (excluding bonuses), in the three months to December before falling marginally to 3.4% in the three months to January. British employers ramped up their hiring at the fastest pace in more than three years in the three months to January as the country's labour market defied the broader weakness in the overall economy as Brexit approached. The number of people in work surged by 222,000, helping to push down the unemployment rate to 3.9 percent, its lowest rate since 1975. Correspondingly, the total level of vacancies has risen to new highs.

2.3. As for CPI inflation itself, this has been on a falling trend, reaching 1.8% in January before rising marginally to 1.9% in February. However, in the February Bank of England Inflation Report, the latest forecast for inflation over both the two and three year time horizons remained marginally above the MPC's target of 2%.

2.4. The rise in wage inflation and fall in CPI inflation is good news for consumers as their spending power is improving in this scenario as the difference between the two figures is now around 1.5%, i.e. a real terms increase. Given the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months.

Brexit

2.5. The Conservative minority government has so far), been unable to muster a majority in the Commons over its Brexit deal. The EU has set a revised deadline of 31 October 2019 for the House of Commons to propose what form of Brexit it would support. It appears unlikely that there would be a Commons majority which would support a disorderly Brexit or revoking article 50, (cancelling Brexit). If a longer delay were to happen, then it increases the chances of a general election in 2019; this could result in a potential loosening of monetary policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

Eurozone

2.6. Growth has been weak at 0.4% in quarter 2, 0.2% in quarter 3, 0.2% in quarter 4 and likely to be 0.1- 0.2% in quarter 1 of 2019. The annual rate of growth for 2018 was 1.8% but is expected to fall to possibly around half that rate in 2019. The European Central Bank (ECB) ended its programme of quantitative easing purchases of debt in December 2018, which means that the central banks in the US, UK and EU have all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by purchases of debt. However, the downturn in growth in the second half of 2018 and into 2019, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), has prompted the ECB to take new measures to stimulate growth. However, with its refinancing rate already at 0.0% and the deposit rate at -0.4%, it has probably reached the bottom of cutting rates. At its March meeting it said that it expects to leave interest rates at their present levels "at least through the end of 2019", but that is of little help to boosting growth in the near term. Consequently, it announced a third round of TLTROs; this provides banks with cheap borrowing every three months from September 2019 until March 2021 which means that, although they will have only a two-year maturity, the Bank is making funds available until 2023, two years later than under its previous policy. As with the last round, the new TLTROs will include an incentive to encourage bank lending, and they will be capped at 30% of a bank's eligible loans.

USA

2.7. President Trump's massive easing of fiscal policy in 2018 fuelled a (temporary) boost in consumption in 2018 which generated an upturn in the strong rate of growth; this rose from 2.2%, (annualised rate) in quarter 1 to 4.2% in quarter 2, 3.5% in quarter 3 and then back to 2.2% in quarter 4. The annual rate came in at 2.9% for 2018, just below President Trump's aim for 3% growth. The strong growth in employment numbers has fed through to an upturn in wage inflation which hit 3.4% in February, a decade high point. However, CPI inflation overall fell to 1.5% in February, a two and a half year low, and looks to be likely to stay around that number in 2019 i.e. below the Fed's target of 2%. The Fed increased rates another 0.25% in December to between 2.25% and 2.50%, this being the fifth increase in 2018 and the ninth in the upward swing cycle. However, the Fed now appears to be edging towards a change of direction and admitting there may be a need to switch to taking action to cut rates over the next two years. Financial markets are now predicting two cuts of 25 bps by the end of 2020.

China

2.8. Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems.

Japan

2.9. Japan has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

World Growth

2.10. Equity markets are currently concerned about the synchronised general weakening of growth in the major economies of the world: they fear there could even be a recession looming up in the US, though this fear is probably overblown. If there were a major worldwide downturn in growth, central banks in most of the major economies will have limited ammunition available, in terms of monetary policy measures, when rates are already very low in most countries, (apart from the US), and there are concerns about how much distortion of financial markets has already occurred with the current levels of quantitative easing purchases of debt by central banks.

3. OVERALL TREASURY POSITION AS AT 31 MARCH 2019

3.1. The Authority's debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity detailed in the Authority's Treasury Management Practices.

3.2. At the end of 2018-19 the Authority's treasury position was as follows:

SUMMARY	31st March 2018 Principal	Rate/ Return	31st March 2019 Principal	Rate/ Return
Total Debt - PWLB (All fixed rate funding) -Other Long Term Liabilities Total	*£25.631m* *£1.299m* *£26.930m*	*4.233%*	*£25.537m* *£1.209m* *£26.747m*	*4.235%*
CFR	*£26.929m*		*£26.747m*	
Over/(under) borrowing	*(0.001)m*		*£0.000m*	
Total Investments	*£37.307m*	*0.55%*	*£38.476m*	*0.83%*
NET DEBT	***£(10.377)m***		***£(11.729)m***	

3.3. The maturity structure of the debt portfolio was as follows:

	31 March 2018 actual	2018/19 original limits	31 March 2019 actual
Under 12 months	£0.093m	£7.661	£0.093
12 months and within 24 months	£0.093m	£7.661	£0.593
24 months and within 5 years	£1.180m	£12.769	£1.080
5 years and within 10 years	£4,213m	£19.153	£3.831
Over 10 years	£20.033m	£25.537	£19.940

4. STRATEGY FOR 2018-19

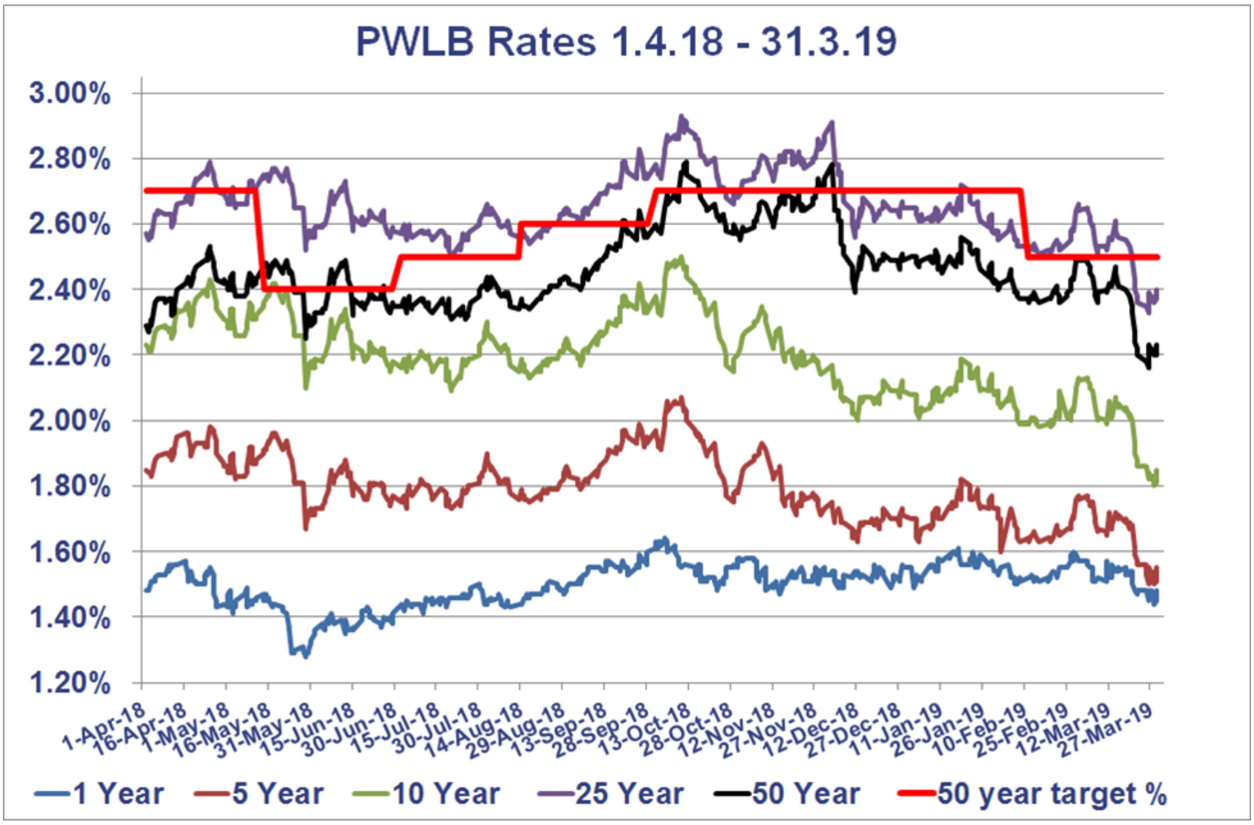
4.1. The expectation for interest rates within the treasury management strategy for 2018/19 anticipated that Bank Rate would not start rising from 0.50% until quarter 4 and not to rise above 1.25% by quarter 1 2021. There would also be gradual rises in medium and longer term fixed borrowing rates during 2018/19 and the two subsequent financial years. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

4.2. In this scenario the strategy, in line with Capital Requirements, was to avoid any new borrowing and bring the level of external loans in line with the Capital Financing Requirement as at 31 March 2019. Opportunities to reschedule or repay loans would be reviewed to reduce external borrowing where viable. If short term interest rates remain low, the Authority will borrow internally to avoid the cost of holding higher levels of investment and to reduce counterparty risk.

5. BORROWING

Public Works Loan Board (PWLB) borrowing rates 2018-19

5.1. The graphs and tables for PWLB rates show, for a selection of maturity periods, the average borrowing rates, the high and low points in rates, spreads and individual rates at the start and the end of the financial year.



	1 Year	5 Year	10 Year	25 Year	50 Year
02/04/2018	1.48%	1.85%	2.23%	2.57%	2.29%
29/03/2019	1.48%	1.55%	1.85%	2.40%	2.23%
Low	1.28%	1.56%	1.86%	2.36%	2.20%
Date	29/05/2018	22/03/2019	22/03/2019	22/03/2019	22/03/2019
High	1.64%	2.07%	2.50%	2.93%	2.79%
Date	04/10/2018	10/10/2018	10/10/2018	10/10/2018	12/10/2018
Average	1.50%	1.80%	2.20%	2.66%	2.47%

DSFRA Borrowing Strategy

Prudential Indicators

5.2. It is a statutory duty for the Authority to determine and keep under review the "Affordable Borrowing Limits". The Authority's' approved Prudential Indicators (affordability limits) are outlined in the approved Treasury Management Strategy.

5.3. During the financial year the Authority operated within the treasury limits and Prudential Indicators set out in its annual Treasury Strategy Statement. The outturn for the Prudential Indicators is shown in Appendix A.

Authority borrowing during and at the end of 2018-19

5.4. No new borrowing was taken out in 2018-19 to support capital spending and therefore, because repayments of £0.093m loan principal have been made in year, the value of loans outstanding has decreased to £25.537m during the year. A summary of the loan (debt) position of the Authority is given in the table below. All existing borrowing has been taken out at Fixed Interest Rates.

5.5. In order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Authority should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2017/18) plus the estimates of any additional capital financing requirement for the current (2018/19) and next two financial years. This essentially means that the Authority is not borrowing to support revenue expenditure. This indicator allowed the Authority some flexibility to borrow in advance of its immediate capital needs in 2018/19.

5.6. It is noted that the external borrowing figure of £25.537m as 31 March 2019 is the same as the Capital Financing Requirement (CFR), within rounding tolerance, which means that there is no over-borrowing position at the year-end. The Authority has complied with this prudential indicator. The table below demonstrates how the CFR is calculated and shows the CFR for 2018-19.

Capital Financing Requirement (£m)	31 March 2018 Actual	31 March 2019 Budget	31 March 2019 Actual
Opening balance	27.098	26.929	26.930
Add borrowing applied in year	1.962	1.911	1.911
Less MRP/VRP*	2.056	2.004	2.004
Less PFI & finance lease repayments	0.075	0.090	0.090
Closing balance	26.930	26.746	26.747

5.7. No rescheduling was done during the year as the average differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Summary of loan movements during 2018-19	Amount £m
Value of loans outstanding as at 1/4/2018	**26.631**
Loans taken during 2018-19	0.00
Loans repaid upon maturity during year	(0.093)
Loans rescheduled during year	0.00
Total value of loans outstanding as at 31/3/2019	**25.537**

6. INVESTMENTS

Authority Investment Strategy

6.1. The Authority's Annual Investment Strategy, which is incorporated in the Treasury Management Strategy Statement, outlines the Authority's investment priorities as follows:

- Security of Capital
- Liquidity
- Yield

6.2. The Authority will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs, but also to seek out value available in periods up to 12 months with highly credit rated financial institutions, using our suggested creditworthiness approach, including a minimum sovereign credit rating, and Credit Default Swap (CDS) overlay information.

Authority Investments during and at the end of 2018-19

6.3. No institutions in which investments were made during 2018-19 had any difficulty in repaying investments and interest in full during the year and the Authority had no liquidity difficulties.

6.4. A full list of investments held as at 31 March 2019 are shown in the table overleaf:

6.5.

Counterparty	Maximum to be invested	Amount Invested	Call or Term	Period invested	Interest rate(s)
	£m	£m			
Aberdeen Standard Investment	5.000	0.150	C	Instant Access	Variable
		0.925	C	Instant Access	Variable
Bank of Scotland	7.000	3.400	T	12 mths	0.90%
		1.500	T	12 mths	0.90%
Barclays FIBCA	8.000	0.001	C	Instant Access	Variable
Eastleigh Burough Council	5.000	1.500	T	6 mths	0.97%
Goldman Sachs	7.000	2.000	T	6 mths	1.08%
		5.000	T	6 mths	1.20%
Santander	7.000	3.000	T	12 mths	0.94%
		1.000	T	6 mths	0.90%
		1.000	T	6 mths	1.00%
Standard Chartered	7.000	2.000	T	6 mths	0.96%
		5.000	T	9 mths	0.98%
Sumitomo Mitsui	7.000	5.000	T	6 mths	0.96%
		2.000	T	3 mths	0.80%
Thurrock Borough Council	5.000	3.500	T	12 mths	0.97%
		1.500	T	12 mths	1.09%
Total amount Invested		**38.476**			

Funds available for investment are on a temporary basis, the level of which are dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme.

Benchmark – 3 month LIBID	**Average level of funds available for Investment £m**	**Benchmark Return**	**Authority Performance**	Investment Interest Earned £m
Quarter 1	36.284	0.53	0.71	(0.021)
Quarter 2	45.041	0.61	0.86	0.043
Quarter 3	44.274	0.79	0.92	0.095
Quarter 4	41.140	0.83	1.02	0.250
2018/19	41.702	0.69	0.83	0.345

6.6. The amount of investment income earned of £0.345m has exceeded the target by £0.201m as a result of levels of fund available for investment during the year being higher than anticipated and returns exceeding benchmark.

7. SUMMARY

7.1. In compliance with the requirements of the CIPFA Code of Practice of Treasury Management, this report provides Members with a summary report of the treasury management activities during 2018-19. As is indicated in this report, none of the Prudential Indicators have been breached, and a prudent approach has been taken in relation to investment decisions taken during the year, with priority being given to liquidity and security over yield.

7.2. Continued uncertainty in the aftermath of the 2008 financial crisis and with unusual Brexit conditions promoted a cautious approach, whereby investments continued to be dominated by risk considerations resulting in relatively low returns compared to borrowing rates. Even so, the Authority is able to report that its returns are above the London Inter-Bank Bid Rate 3 month rate, the benchmark return for this type of short term investments.

AMY WEBB
Director of Finance (Treasurer)

APPENDIX A TO REPORT RC/19/8

PRUDENTIAL INDICATOR	2017-18 £m actual	2018-19 £m approved	2018-19 £m Actual
Capital Expenditure			
TOTAL	2.889	6.423	2.878
Ratio of financing costs to net revenue stream			
Non – HRA	4.18%	4.03%	3.83%
Capital Financing Requirement as at 31 March (borrowing only)			
TOTAL	26.929	26.747	26.747
Annual change in Cap. Financing Requirement			
TOTAL	(0.169)	(0.182)	(0.182)
TREASURY MANAGEMENT PRUDENTIAL INDICATORS			
	£m	**£m**	**£m**
Authorised Limit for external debt -			
Borrowing	27.005	27,007	27.007
other long term liabilities	1.439	1,359	1.359
TOTAL	28.445	28.367	28.367
Operational Boundary for external debt -			
Borrowing	25.724	25.731	25.731
other long term liabilities	1.374	1.299	1.299
TOTAL	27.098	27.029	27.029
Actual external debt	26.929		26.747

	Actual 31st March 2019	upper limit %	lower limit %
Limits on borrowing at fixed interest rates	100%	100%	70%
Limits on borrowing at variable interest rates	0%	30%	0%
Maturity structure of fixed rate borrowing during 2018-19			
Under 12 months	0.37%	30%	0%
12 months and within 24 months	2.32%	30%	0%
24 months and within 5 years	4.23%	50%	0%
5 years and within 10 years	15.66%	75%	0%
10 years and above	78.08%	100%	50%

APPENDIX B TO REPORT RC/19/8

Glossary of Terms

ALMO: an Arm's Length Management Organisation is a not-for-profit company that provides housing services on behalf of a local authority. Usually an ALMO is set up by the authority to manage and improve all or part of its housing stock.

LAS: Link Asset Services, Treasury solutions – the council's treasury management advisers.

CE: Capital Economics - is the economics consultancy that provides Link Asset Services, Treasury solutions, with independent economic forecasts, briefings and research.

CFR: capital financing requirement - the council's annual underlying borrowing need to finance capital expenditure and a measure of the council's total outstanding indebtedness.

CIPFA: Chartered Institute of Public Finance and Accountancy – the professional accounting body that oversees and sets standards in local authority finance and treasury management.

CPI: consumer price inflation – the official measure of inflation adopted as a common standard by countries in the EU. It is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. It is calculated by taking price changes for each item in the predetermined basket of goods and averaging them.

ECB: European Central Bank - the central bank for the Eurozone
EU: European Union
EZ: Eurozone -those countries in the EU which use the euro as their currency

Fed The Federal Reserve, often referred to simply as "the Fed," is the central bank of the United States. It was created by the Congress to provide the nation with a stable monetary and financial system.

FOMC: the Federal Open Market Committee – this is the branch of the Federal Reserve Board which determines monetary policy in the USA by setting interest rates and determining quantitative easing policy. It is composed of 12 members--the seven members of the Board of Governors and five of the 12 Reserve Bank presidents.

GDP: gross domestic product – a measure of the growth and total size of the economy.

G7: the group of seven countries that form an informal bloc of industrialised democracies--the United States, Canada, France, Germany, Italy, Japan, and the United Kingdom--that meets annually to discuss issues such as global economic governance, international security, and energy policy.

Gilts: gilts are bonds issued by the UK Government to borrow money on the financial markets. Interest paid by the Government on gilts is called a yield and is at a rate that is fixed for the duration until maturity of the gilt, (unless a gilt is index linked to inflation); yields therefore change inversely to the price of gilts i.e. a rise in the price of a gilt will mean that its yield will fall.

HRA: housing revenue account.

IMF: International Monetary Fund - the lender of last resort for national governments which get into financial difficulties.

LIBID: the London Interbank Bid Rate is a bid rate; the rate bid by banks on deposits i.e., the rate at which a bank is willing to borrow from other banks. It is the "other end" of the LIBOR (an offered, hence "ask" rate, the rate at which a bank will lend).

MHCLG: the Ministry of Housing, Communities and Local Government -the Government department that directs local authorities in England.

MPC: the Monetary Policy Committee is a committee of the Bank of England, which meets for one and a half days, eight times a year, to determine monetary policy by setting the official interest rate in the United Kingdom, (the Bank of England Base Rate, commonly called Bank Rate), and by making decisions on quantitative easing.

MRP: minimum revenue provision -a statutory annual minimum revenue charge to reduce the total outstanding CFR, (the total indebtedness of a local authority).

PFI: Private Finance Initiative – capital expenditure financed by the private sector i.e. not by direct borrowing by a local authority.

PWLB: Public Works Loan Board – this is the part of H.M. Treasury which provides loans to local authorities to finance capital expenditure.

QE: quantitative easing – is an unconventional form of monetary policy where a central bank creates new money electronically to buy financial assets, like government bonds, (but may also include corporate bonds). This process aims to stimulate economic growth through increased private sector spending in the economy and also aims to return inflation to target. These purchases increase the supply of liquidity to the economy; this policy is employed when lowering interest rates has failed to stimulate economic growth to an acceptable level and to lift inflation to target. Once QE has achieved its objectives of stimulating growth and inflation, QE will be reversed by selling the bonds the central bank had previously purchased, or by not replacing debt that it held which matures. The aim of this reversal is to ensure that inflation does not exceed its target once the economy recovers from a sustained period of depressed growth and inflation. Economic growth, and increases in inflation, may threaten to gather too much momentum if action is not taken to ‘cool’ the economy.

RPI: the Retail Price Index is a measure of inflation that measures the change in the cost of a representative sample of retail goods and services. It was the UK standard for measurement of inflation until the UK changed to using the EU standard measure of inflation – CPI. The main difference between RPI and CPI is in the way that housing costs are treated. RPI is often higher than CPI for that reason.

TMSS: the annual treasury management strategy statement report that all local authorities are required to submit for approval by the full council before the start of each financial year.

VRP: a voluntary revenue provision to repay debt, in the annual budget, which is additional to the annual MRP charge, (see above definition).