MIDDLESBROUGH COUNCIL

Report of:	Strategic Director - Finance, Governance & Support – James Bromiley Executive Member – Finance & Governance – Cllr Chris Hobson

Submitted to:	Executive – 8 October 2019

Subject:	Treasury Management Outturn Report – 2018/19

Summary

Proposed decision(s)
That the Executive notes the year–end results on treasury management activity for 2018/19.

Report for:	Key decision:	Confidential:	Is the report urgent?[1]
Information	Not Applicable	The report is not confidential and can be made publicly available.	No

Contribution to delivery of the 2018-22 Strategic Plan		
Business Imperatives	**Physical Regeneration**	**Social Regeneration**
Treasury Management contributes to good quality financial management of the Council's overall cash resources, and mitigates risks attached with high value financial transactions.	Treasury Management facilitates cash being available to pay for the Council's Investment Strategy and the benefits of this long term funding for the town.	Treasury Management facilitates cash being available to pay for the Council's Social Regeneration plans & priorities.

Ward(s) affected
No direct implications on any individuals wards within the Borough.

[1] Remove for non-Executive reports

What is the purpose of this report?

1. This report provides information relating to the regulation and management of the Council's borrowing, investments and cash flow activities for the financial year, 2018/19. It is a requirement of the Charted Institute of Public Finance & Accountancy (CIPFA) Code of Practice on Treasury Management that a local authority reports annually on its performance against its approved strategy. This was agreed by full Council on 7 March 2018 as part of the Revenue Budget, Council Tax, Medium Term Financial Plan & Capital Strategy report.

2. The report also seeks to provide the year-end position against the prudential indicators which were approved as part of the above Budget report. These indicators allow Members to understand whether the Investment Strategy (Capital Programme) of the Council is affordable, sustainable and prudent.

Why does this report require a Member decision?

3. The report is for information purposes only.

Report Background

4. The objective of Treasury Management is to manage and control the Council's cash flows, its borrowings and its investments, and other banking activities. This needs to be done in such a way as to mitigate the associated risks involved and to achieve a high level of support to the Strategic Plan that is consistent with those risks. Treasury Management transactions are some of the largest individual expenditure and income items made by the Council each year and as such making good quality transparent decisions and ensuring that these are consistent with the strategies in place is very important.

5. The Executive on 23 April 2002 approved the adoption of the CIPFA Code of Practice on Local Authority Treasury Management, with the Code being deemed as best practice for Councils to follow in this area. It recommends that a policy statement & annual strategy for treasury management, plus a set of Prudential Indicators for capital finance, are adopted before the start of each financial year and that these are an integral part of the overall budget strategy and medium term financial planning approach. The Code has been updated several times since 2002 by CIPFA but the core elements continue to be similar and the revision of the annual strategy by the Council each year ensures ongoing compliance.

6. By governing the Council's treasury activities in a robust way, it is possible to reduce the costs involved in funding the capital programme and to also ensure that the risks of placing any surplus funds with external financial institutions is minimised. These are both key elements of the Treasury Strategy approved in March 2018. The Council had a capital financing budget of £8.243m in 2018/19 to support the associated borrowing and investment costs.

7. Compliance with the locally set suite of Prudential Indicators, set as part of the 2018/19 budget strategy, provides evidence of a well-managed and affordable capital programme and that the Council is managing its strategic financial plans in line with its original budget assumptions.

Investments

8. The Council throughout the financial year has a fluctuating level of cash balances which arise as a result of timing differences between revenue and capital income being received and financial commitments on these plans being paid for. This cash, if not needed immediately, can be invested for periods between one day and one year via various types of financial instruments. These amounts are placed in line with our approved strategy of investing in quality financial institutions with the security, liquidity and yield being fully considered prior to making any investment decisions. This is also in line with appropriate government regulations in this area.

9. The total interest received on investing surplus cash balances within 2018/19 was £0.155M. This was achieved from holding an average daily cash balance of £19.940m and at an average interest rate of 0.785%, marginally above the prevailing bank rate of 0.75%, which is the normal annual target. The cash balances of the Council during the year fluctuated between £10m and £30m depending on income received and commitments. These were supported by drawing down both short term and long term borrowing where needed.

10. The investments held at the end of 2018/19 totalled £13.600m. There is a requirement for local authorities, as part of the current European financial instruments directive, that to be a professional investor your cash balances should remain in excess of £10.000m. The Council maintained this at all times during the year and as a result has continued with its professional status where it has very limited financial regulation before making its own borrowing and investment decisions. Of the £13.6m available, £10.0m is held in 6 monthly deposits with other local authorities, with the remaining £3.6m held on call for liquidity purposes.

11. The Council has managed its cash balances at a relatively minimal level over the past few financial years. This has been a strategic budget decision as it has been cheaper to use internal resources (generally reserves and other forms of capital cash) to finance the Council's investment strategy while the bank base rate has been at historical lows, rather than to use external long term borrowing. This policy has resulted in significant capital financing savings to the revenue budget position since the banking crisis in 2008.

12. At the start of the financial year, cash balances were £20.111m. The reduction to £13.600m reflects the use of earmarked reserves to part fund the revenue outturn position in 2018/19, as well as other working capital changes. Income related to reserves is usually received in a previous financial year so any use in the current year reduces the cash resources available.

External Borrowing

13. The Council can borrow money from banks, local authorities and the public works loan board (a government agency that acts as a cheap rate borrowing facility to the public sector) to fund its capital programme. By doing this it needs to operate within the limits set as part of the CIPFA Prudential Code for Capital Finance. This, again, is seen as best practice in relation to local authorities and how they run their treasury activities. The Council uses an external treasury management advisor, Arlingclose, to help develop its treasury management strategy and practices. They advise the Council on all borrowing and investment decisions taken during the financial year and any associated risk involved in these transactions.

14. Current external borrowing stands at £162.547m (up from £152.366m at 31 March 2018). This increase is due to £21.000m being needed in 2018/19 from the Public Works Loan Board to finance the approved capital programme, plus any cash flow demands from delivering the revenue budget, less any debt maturing. The debt portfolio is split between £13.203m of short term debt repayable during 2019/20 and £149.344m which matures at various intervals between 2020/21 and 2065/66.

Borrowing	**Amount (£m)**	**Average Rate (%)**	**Average Life (Years)**
Fixed Rate Funding			
Public Works Loan Board	114.547	2.93%	25.0
Market (Lender Option Borrower Option)	28.000	5.85%	23.8
Market (Fixed)	20.000	2.63%	4.75
Total	**162.547**	**3.39%**	**22.3**

Prudential Indicators

15. Part of the CIPFA Code for capital finance requires local authorities to operate a system of self-regulation over capital and treasury management activities through the use of locally set prudential indicators. These indicators aim to demonstrate that the financial borrowing plans for the Council are affordable, sustainable and prudent in view of the resources available and are set by full Council as part of the budget strategy each financial year.

16. The indicators cover a range of performance criteria on capital finance, from total capital expenditure incurred, the level of the capital financing requirement (the underlying need of the Council to borrow), affordable limits in relation to total borrowing, external debt and the ratio of financing costs to the net revenue budget. The outturn position against these indicators (below) shows that these prudential indicators have been well managed within the parameters previously set.

Prudential Indicator	**Quarter 3 Limit 2018/19 £m**	**Outturn 2018/19 £m**	**Indicator Met?**
Capital Investment Indicators			
Capital Expenditure	38.814	31.507	Yes
Capital Financing Requirement	198.852	195.235	Yes
External Debt Indicators			
Authorised Limit for External Debt	235.900	182.547	Yes
Operational Boundary for External Debt	215.500	162.547	Yes
External Debt	162.324	162.547	Yes
Affordability Indicators			
Capital Financing Budget	8.243	7.377	Yes
Financing Costs as a % of the Net Revenue Budget	7.4%	6.6%	Yes

17. The capital programme for 2018/19 reduced from a starting position of £44.4m to an outturn position of £31.5m. This reduction reflects the complexity of achieving and delivering capital schemes and the various planning, legal and commercial decisions that are required. Some of this reduction in the capital programme will have been financed by prudential borrowing. As a result the capital financing assumptions and limits have changed and the overall need to borrow for capital purposes is lower than expected.

18. The external debt totals are all well below the initial prudential indicators set by the Council. This reflects no opportunities being available to refinance any existing external debt. The Council retained an amount of £40.000m within these limits to ensure it had the necessary capacity to consider any financial institutions who may want to allow us to repay debt earlier than planned. Due to the economic conditions and current uncertainty in the financial markets and with interest rates remaining low, there were no refinancing opportunities for the Council in 2018/19.

19. When debt levels are below the need to borrow, this position is known as ‘under borrowing’. Most local authorities are currently under borrowed to some extent as it is cheaper to use existing internal resources than borrow externally. The Council expected to be £36.5m under its capital financing requirement at Quarter 3 2018/19. However, due to the underachievement on the capital programme in the final quarter, with some schemes funded by borrowing being realigned into later years, the final position at 31st March 2019 was £32.7m under borrowed. This change will be factored into future strategic decisions around the capital programme.

Capital Financing Budget

20. Due to a combination of borrowing for the year being achieved at lower levels than originally budgeted for, no debt refinancing activities and a number of invest to save schemes being part of this year’s programme, there was an underspend against this budget of £0.866m which helped to manage the final revenue budget position. The total spend on capital financing in 2018/19 was £7.4m or 6.6% of the net revenue budget of £111m.

Future Years Implications

21. In terms of the affordability of the capital programme going forwards and its impact on the treasury management plans, the Council has previously set out a ‘nominal’ cap on its capital financing costs of 10% of its annual revenue budget. The 2019/20 set of prudential Indicators, approved on 4th March 2019, show that this % will increase significantly during this year, up to around 8.5% - 9% given the capital commitments already agreed. Members will therefore need to be prudent around the authority’s plans going forward and any significant future capital investment or borrowing decisions that are taken.

What decision(s) are being asked for?

22. That the Executive notes the year–end results on treasury management activity for 2018/19.

Why is this being recommended?

23. It is best practice for Members to review the performance on treasury management against the approved plans for the Council.

Other potential decisions and why these have not been recommended

24. Not applicable.

Impact(s) of recommended decision(s)

Legal

25. The Council's treasury management arrangements are compliant with legal requirements under the Local Government Act 2003 and the best practice codes issued by CIPFA on Treasury Management and Capital Finance.

Financial

26. The financial implications relating to the Council's treasury management activities are set out in the report.

Policy Framework

27. As part of the Council's financial procedure rules, the responsibility for monitoring treasury management policies & practices is delegated to the Executive. The responsibility for the execution and administration of daily treasury management decisions rests with the Strategic Director of Finance, Governance and Support (as the Section 151 Officer).

Equality and Diversity

28. No negative differential impact on diverse groups and communities is anticipated from the policies or strategies covered by this report.

Risk

29. Risk is a fundamental part of treasury management for a local authority due to the size of the financial transactions and the reputational aspects that poor practice may bring. Members will recall the consequences of a number of local authorities investing in Icelandic banks in 2008 and these banks subsequently collapsing which put the repayment of their short term deposits at risk. However, fortunately this did not affect Middlesbrough Council. As well as this type of credit risk, there is risk attached to any external borrowing decision as interest rates may change over the period of the loan. There is also liquidity risk in ensuring that cash balances are appropriate at all times to pay staff and suppliers and ensuring that the Council does not become overdrawn in its bank accounts.

30. Given the extensive and significant nature of the risks involved in treasury management, the local authority code recommends that Councils maintain a set of treasury management practices (TMP) covering processes, staffing, and training and how these help to manage these risks. This has been in place since 2002 with the latest iteration of Middlesbrough's TMPs being approved by full Council in March 2019 as Appendix 9 to the budget report for 2019/20.

Actions to be taken to implement the decision(s)

31. No decisions are required within this report.

Appendices

32. There are no appendices to this report.

Background papers

33. No background papers were used in the preparation of this report.

Contact: Justin Weston, Chief Accountant, Finance, Governance & Support
Email: justin_weston@middlesbrough.gov.uk