Part A **Report to: Audit Committee**

Date of meeting: Thursday, 30 July 2020

Report author: Interim Head of Finance

Title: Treasury Management Annual Report 2019/20

1. Summary

This report gives details of the 2019/20 year-end review of the Treasury Management function.

2.0 Risks

2.1

Nature of risk	**Consequence**	**Suggested Control Measures**	**Response** (treat, tolerate, terminate or transfer)	**Risk Rating** (combination of severity and likelihood)
Failure to follow the approved TM Strategy	Non-compliance can result in penalties and potential financial loss	Daily cashflow reconciliations and regular updates from external advisors	Treat	4

3. Recommendations

3.1 That the Committee notes the Annual Treasury Management Report.

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Report approved by: Alison Scott, Director of Finance

4. Detailed Proposal

4.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as: “the management of the local authority’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks”.

4.2 The Council’s 2019/20 Treasury Management Strategy (TMS) as approved by Council in January 2019 has the primary objectives of safeguarding the repayment of the principal and interest of its investments on time, and then ensuring adequate liquidity, with the investment return being the final objective.

4.3 This report provides the Committee with an overview of Treasury Management performance for 2019-20.

4.4 The Council has appointed treasury advisors to assist with our treasury management, Link Asset Services.

The Council’s Capital Position (Prudential Indicators)

4.5 The Council’s capital expenditure plans are one of the key drivers of treasury management activity. The outputs of the capital expenditure plans are reflected in prudential indicators, which are designed to assist members’ overview and confirm capital expenditure plans.

Capital Financing Requirement (CFR), External Debt and Operational Boundary

- **CFR** measures the Council’s underlying need to borrow for capital purposes, representing the Council’s total outstanding indebtedness.
  External Debt (borrowing) may not exceed the CFR except in the short-term.

- **The Operational Boundary** is a limit on the level of external debt set by the Council. This is set based on the most likely prudent (i.e. not worst-case scenario) estimate of total external debt, in line with statutory guidance.

  External debt may exceed the Operational Boundary, but may not exceed the Authorised Limit for external debt, which is set at a higher level and provides further headroom for unusual cash movements or refinancing.

The CFR and Operational Boundary estimates are shown below:

Prudential Indicator	2019/20 Original Estimate	2019/20 Revised Estimate (mid-year)	2019/20 Outturn
Capital Financing Requirement (Loans)*	£57.2m	£57.2m	£43.15
External Debt / the Operational Boundary			
Borrowing (Net debt)	£25.0m	£25.0m	£15.0m

*Loans CFR is the level of underlying debt requiring finance. The CFR related to the Croxley Business Park non-treasury investment is excluded as this is financed under a leasing arrangement.

Borrowing has been lower than expected due to re-phasing of the capital programme as a result of slower than projected delivery of projects.

Limits to Borrowing Activity

4.6 The first key control over the treasury activity is a Performance Indicator (PI) to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. External borrowing should not exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2018/19 and next two financial years. This allows some flexibility for limited early borrowing for future years.

The Operational Boundary

4.7 This PI, which is required to be set and revised by Members, is the limit beyond which external borrowing is not normally expected to exceed. In most cases this would link directly to the authority’s plans for capital expenditure, its estimates for CFR and its estimate of cashflow requirements for the year for all purposes.

Operational Boundary For External Debt	2019/20 Original Indicator	2019/20 Revised Indicator	2019/20 Net Debt Outturn
Borrowing (net debt)	£25.0m	£25.0m	£15.0m

The Authorised Limit

4.8 This PI, which is required to be set and revised by Members, controls the overall level of borrowing and represents the limit beyond which borrowing is prohibited. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Authorised Limit For External Debt	2019/20 Original Indicator	2019/20 Revised Indicator	2019/20 Net Debt Outturn
Borrowing (net debt)	£30.0m	£30.0m	£15.0m

Investment Portfolio 2019/20

4.9 In accordance with the CIPFA Prudential Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. As set out in Section 2 of the Code, it is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low, in line with the Bank of England base rate.

4.10 In response to the Covid-19 public health emergency, the Bank reduced base rate to 0.10% in March 2020 in order to provide support to the UK economy. It now appears likely that the crisis will lead to a global recession with prospects for recovery remaining highly uncertain. Given this risk environment, investment returns are likely to remain very low for some time to come.

4.11 The Council held £13.129m of investments as at 31 March 2020 (see table below). This information is reported in the monthly Members Information Bulletin

Institution	Principal (£'000)
Lloyds Bank – Current Account	11,129
UK Debt Management Office	2,000
Total	**13,129**

4.12 The approved limits within the Annual Investment Strategy were not breached during 2019/20.

Security

4.13 The Council uses benchmarks as simple guides to maximum risk, and these may be breached from time to time, depending on movements in interest rates and counterparty criteria. Any breach of the benchmarks will be reported, with supporting reasons, in this report. There were no breaches to report during 2019/20.

4.14 In line with the TMS, the Council has managed to invest with those institutions who offered the best rate and the investment portfolio is above the overall benchmark during the year to date.

Liquidity

4.15 The Council set liquidity facilities/benchmarks to maintain:

- Authorised bank overdraft of £nil.
- Liquid short term deposits of at least £5m available with a week's notice.

The liquidity arrangements were adequate during the year.

Yield

4.16 The approved benchmark measure of yield is a return of 0.12% above the average bank rate. The bank rate was 0.75% until 11 March 2020, when it was reduced to 0.25%. The rate was further reduced to 0.10% on 19 March. The return for 2019/20 was equivalent to 0.59%, against a benchmark rate of 0.84% for the year. Performance remained below benchmark for the period due to difficult investment conditions and the low levels of surplus cash.

4.17 The Council keeps all investments short term. There are no sums within the TMS invested for greater than 364 days. Counterparties have been downgraded over the past few years; most investments have been limited to a 6 months period. This has resulted in lower interest rates being achieved. The budget for interest earned on treasury investments for 2019/20 is £150k; interest received and accrued to the end of March 2020 was £95k.

4.18 The current investment counterparty criteria selection approved in the TMS is being met.

Credit Ratings

4.19 Credit rating information is supplied by our treasury consultants, Link Asset Services, on all counterparties that comply with the Council's criteria. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing.

4.20 The Council's Treasury Management Strategy sets out the risks that it is seeking to manage. These risks are:

- **Liquidity Risk**
  That the Council may not have the cash it needs on a day to day basis to pay its bills. This risk is managed through forecasting and the retention by the Council of an adequate working capital balance. In addition, through the Public Works

Loan Board and other organisations, the Council is able to access short term borrowing, usually within 24 hours.

- **Interest Rate Risk**
  That the costs and benefits expected do not materialise due to changes in interest rates. This risk is managed through the placing of different types and maturities of investments, the forecasting and monitoring of the interest budget (with assistance from the Council's retained advisors).

- **Exchange Rate Risk**
  That losses or gains are made due to fluctuations in the prices of currency. The Council does not engage in any significant non-sterling transactions.

- **Credit and Counterparty Risk**
  That the entity holding Council funds is unable to repay them when due. This risk is managed through the maintenance of a list of authorised counterparties, with separate limits to ensure that the exposure to this risk is limited

- **Refinancing Risk**
  That the loans taken by the Council will become due for repayment and need replacing at a time when there is limited finance available or interest rates are significantly higher. The timing of loan maturities is monitored along with interest rate forecasts. Officers ensure that due dates are monitored and seek advice from the Council's advisors about when to raise any finance needed.

- **Legal and Regulatory Risk**
  That the Council operates outside its legal powers. This risk is managed through the Council's training and development of Officers involved in Treasury Management, the independent oversight of Internal and External Audit, and the advice (for example on the contents of this strategy) taken from the Council's Treasury advisors.

- **Fraud, Error and Corruption**
  The risk that losses will be caused by impropriety or incompetence is managed through the controls in the Council's financial procedures. For example, the segregation of duties between those making investment decisions and those transferring funds

- **Market Risk**

That the price of investments held fluctuates, principally in secondary markets. The majority of the Council's investments are not traded, but where they are (e.g. Property investment portfolio) the main investments' value comes from the income they generate which is generally long term and secure

5. Implications

5.1 Financial

5.1.1 The Shared Director of Finance comments that this report provides formal assurance on the Council's compliance with its Treasury Management Strategy during the year.

5.2 **Legal Issues** (Monitoring Officer)

5.2.1 The Head of Democracy and Governance comments that there are no legal implications of this report.

5.3 Equalities, Human Rights and Data Protection

5.3.1 There are no implications of this report.

4.4 Staffing

5.4.1 There are no implications of this report.

5.5 Accommodation

5.5.1 There are no implications of this report.

5.6 Community Safety/Crime and Disorder

5.6.1 There are no implications of this report.

5.7 Sustainability

5.7.1 There are no implications of this report.

Appendices

- None

Background papers

Capital Strategy and Treasury Management Strategy 2019/20 (published as part of the 2019/20 Budget)