

Meeting of the Council – 7th October, 2019

Report of the Audit and Standards Committee

Treasury Management

Purpose of Report

1. To outline treasury activity during the financial year 2018/19 and in the current financial year up to late August.

Recommendation

2. That the report be noted.

Background

3. The Treasury Management strategy for 2019/20 has been underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2017. The Code recommends that members are informed of Treasury Management activities at least twice a year. This report ensures that the Council is embracing best practice in accordance with CIPFA's recommendations.
4. Treasury Management entails the management of the Council's cash flows, its borrowings and investments, the management of the associated risks and the pursuit of the optimum performance or return consistent with those risks.
5. The Council undertakes treasury management activity on its own behalf and as administering authority for the West Midlands Debt Administration Fund (*WMDAF*). We are responsible for administering capital funding of approximately £768m on our own account and another £121m on behalf of other West Midlands councils in respect of the WMDAF. The treasury function is governed by the Council's Treasury Policy Statement and Treasury Management Practices.

Treasury activity in 2018/19 on the Dudley fund

6. Our treasury activities were undertaken in the context of the Treasury Strategy Statement 2018/19 approved by Audit and Standards Committee and Full Council in February 2018. The Strategy Statement stated:

“The primary factor in determining whether we undertake new long-term borrowing will be cash flow need. We will seek to minimise the time between borrowing and anticipated cash flow need, subject to the need to maintain day to day liquidity”

7. In 2018/19 our investments averaged around £33.6 million (with significant day to day variation as a result of cash flow). The average return on these investments was 0.61% (excluding the long term investment with Salford City Council, the average return was 0.45%). The majority of our investments were for less than one month or were in call accounts¹. All investments were placed with institutions that satisfied the criteria for credit-worthiness set out in the Treasury Strategy Statement 2018/19. Our investment activity for 2018/19 is set out in more detail in Appendix 1.
8. The average value of long-term borrowings in 2018/19 was £645.9 million. The average rate of interest on these borrowings was 3.50% (compared to 3.46% in 2017-18 due to the increase in bank base rates which affected the cost of market loans). The loans were due to mature on dates ranging from 2019 to 2061.
9. In 2018/19 we took out 6 long term market loans. The average value of these loans was £5.5m at an average rate of 1.1%, for an average duration of 23 months.
10. Due to cash flow requirements in 2018/19, it was necessary to undertake short term borrowing on 2 occasions, both for £5.0 million at an average rate of 0.85% for average duration of 6 days.

Treasury activity in 2018/19 on the WMDAF

11. It was necessary to undertake short term borrowing on 4 occasions for cashflow purposes, at an average value of £3.0million at 0.81% for an average duration of 110 days. We also made 3 investments in 2018/19 for the WMDAF for an average value of £3.0 million at 0.56% for 40 days.

Performance comparisons 2018/19

12. Our treasury management advisors Link Asset Services have compared our treasury performance with their other clients using borrowing and investment data at financial year end. The results are summarised in the table below:

¹ A call account is a deposit account with a financial institution without a fixed maturity date. The deposit can be "called" (withdrawn) at any time and deposits can also be made at any time. Call accounts and the specific terms associated with them differ depending upon the bank offering the account.

Performance Benchmarking

	Dudley	Client Average
Gross Borrowing (£M)	639.6	215.5
Investments (£M)	4.0	71.3
Net Borrowing (£M)	635.6	144.2
Gross average borrowing rate (the cost of borrowing, ignoring the return on investments)	3.47%	4.57%
Investment return rate (the return on investments, ignoring the cost of borrowing)	0.65%	0.84%
Net average borrowing rate (a combination of the above, representing the cost of borrowing net of the return on investments)	3.48%	6.41%

13. The data above is based on a snapshot of treasury portfolios at 31st March 2019 and includes long and short term borrowing and investments. Dudley's net cost of borrowing was substantially lower than the average of local authorities in the client group. This is partly because our ratio of gross to net borrowing is higher than other authorities who maintain larger levels of investments which are currently delivering very low yields.
14. It should be remembered that treasury performance measurement is not an exact science. These statistics represent the cumulative effect of decisions dating back over many years and the performance of other local authorities may have been achieved in circumstances different from our own.

Prudential indicators 2018/19

15. The 2003 Prudential Code for Capital Finance in Local Authorities sets out a framework for the consideration and approval of capital spending plans. In so doing, it requires the Council to set a number of prudential indicators, some of which concern matters of treasury management. Appendix 2 outlines those indicators for 2018/19.

Treasury activity 2019/20 to August

16. Treasury activities in the current year have been undertaken in the context of the Treasury Strategy Statement 2019/20 approved by Audit and Standards Committee and Council in February of this year. In that document we anticipated that long term borrowing would be required in the next 12 months due to cash flow need.

17. The Monetary Policy Committee (MPC) has maintained the bank base rate at 0.75% since August 2018. Their most recent inflation report indicated that the economy will slow in 2019/20 and the first estimate of the Gross Domestic Product (GDP) for the second quarter of 2019 indicated that it fell by 0.2%, possibly enhancing the chances of an interest rate cut.
18. Our investments up to the middle of August have averaged around £14.4 million (with significant day to day variation as a result of cash flow). The average return on these investments was 0.85% (excluding the Salford investment the average return is 0.48%). All investments were placed with institutions that satisfied the criteria for credit-worthiness set out in the Treasury Strategy Statement 2019/20. Our investment activity for 2019/20 is set out in more detail in Appendix 3.
19. The average value of long-term borrowings up to late August has been £620.1million. The average rate of interest on Dudley's loans is 3.51%. The maturity dates for the loans range from the current year to 2061. No new long term borrowing has so far been taken out in 2019-20 but for cashflow purposes we have taken out short term loans on 5 occasions with an average value of £5.5m at average rate of 0.73% for an average duration of 11 days.
20. We are monitoring interest rates and cash flow closely and continue to anticipate that some long term borrowing will be required before the financial year end, principally to replace existing loans as they mature.
21. On the WMDAF it has not been necessary to undertake any new borrowing in 2019-20 to date. We have made 1 investment on the WMDAF to date in 2019/20 with the Debt Management Office (DMO) for a value of £4.3m at a rate of 0.52% for 85 days.

Finance

22. Forecasts of performance against budget for treasury management activities are highly sensitive to movements in cash flow and interest rates.

Law

23. These matters are governed by Part IV of the Local Government and Housing Act 1989 and Section 111 of the Local Government Act 1972, which empowers the Council to do anything which is calculated to facilitate or is conducive or incidental to the discharge of its various statutory functions.

Equality Impact

24. The treasury management activities considered in this report have no direct impact on issues of equality.

Organisational Development/Transformation

25. There are no Organisational Development/human resources or Transformation implications associated with this report.

Commercial/Procurement

26. The over-riding purpose of the Council's Treasury Strategy is day to day cash management and not income generation. The strategy prioritises security and liquidity of cash investments over yield. Once those are met we aim to secure the maximum yield from our investments held with the small number of counterparties that meet the strict criteria laid out in our Annual Investment Strategy.

Health, Wellbeing and Safety

27. This report has no direct impact on the Health, Wellbeing and Safety of the Borough's citizens.



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Chair of the Audit and Standards Committee

Investment Activity 2018/19

Counterparty name	Number of investments	Average value £ million	Average rate %	Average duration (days)
Debt Management Office	146	22.54	0.44	18
Santander	N/A	2.81	0.40	Call Account
Bank of Scotland	N/A	4.81	0.57	Call Account
HSBC	N/A	2.91	0.36	Call Account
Salford MDC*	1	0.50	11.25	Matures in 2020

* This is a fixed term deposit of £500,000.00 with Salford MDC at an interest rate of 11.25% that was made in 1985 and is due to mature in 2020.

Prudential indicators relating to treasury management 2018/19

External debt

These indicators are intended to ensure that levels of external borrowing are affordable, prudent and sustainable. The authorised limit for external debt is a statutory limit (section 3 of the Local Government Act 2003) that should not be breached under any circumstances. The operational boundary is a lower threshold allowing for a prudent but not worst case scenario for cash flow.

	£m
Authorised limit for external borrowing	1,067
Operational boundary for external borrowing	895
Outturn - actual external borrowing	822

Interest rate exposures and maturity structure of borrowing and investments

These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates.

	Indicator	Outturn
Upper limit for fixed interest rate exposure	100%	98.36%
Upper limit for variable rate exposure	10%	1.64%
Upper limit of principal maturing in any one year for sums invested for over 364 days	£10m	Nil
Maturity structure of fixed rate borrowing:-		
under 12 months	0-10%	9.52%
12 months and within 24 months	0-10%	8.25%
24 months and within 5 years	0-15%	11.97%
5 years and within 10 years	0-25%	11.08%
10 years and above	40-100%	59.18%

Appendix 3

Investment Activity 2019/20 to August

Counterparty name	Number of investments	Average value £ million	Average rate %	Average duration (days)
Debt Management Office	37	7.97	0.47	9
Santander	N/A	0.03	0.40	Call Account
Bank of Scotland	N/A	1.92	0.65	Call Account
HSBC	N/A	3.99	0.41	Call Account
Salford MDC*	1	0.50	11.25	Matures in 2020

* This is a fixed term deposit of £500,000.00 with Salford MDC at an interest rate of 11.25% that was made in 1985 and is due to mature in 2020.