POLICY RESOURCES & GROWTH COMMITTEE	Agenda Item 79 Brighton & Hove City Council

Subject:		**Treasury Management Strategy Statement 2018/19 - Mid Year Review**	
Date of Meeting:		**06 December 2018**	
Report of:		**Executive Director for Finance & Resources**	
Contact Officer:	**Name:**	**James Hengeveld**	**Tel: 01273 291242**
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Ward(s) affected:		**All**	

FOR GENERAL RELEASE

1. PURPOSE OF REPORT AND POLICY CONTEXT

1.1 The 2018/19 Treasury Management Strategy Statement (TMSS), practices and schedules were approved by Policy, Resources & Growth Committee on 29 March 2018 and full Council on 19 April 2018.

1.2 The TMSS sets out the role of Treasury Management, whilst the practices and schedules set out the annual targets and methods by which these targets will be met. The TMSS includes the Annual Investment Strategy (AIS) which sets out the key parameters for investing council cash funds.

1.3 It is recommended good and proper practice that Members receive half yearly reports and review and endorse treasury management actions during the year. The purpose of this report is to advise of the action taken in the first half of 2018/19.

2. RECOMMENDATIONS:

2.1. That Policy, Resources & Growth Committee notes the key actions taken during the first half of 2018/19 to meet the TMSS and the investment strategy as set out in this report.

2.2. That Policy, Resources & Growth Committee notes the reported compliance with the AIS for the period under review.

2.3. That Policy, Resources & Growth Committee notes that the approved maximum indicator for investment risk of 0.05% has been adhered to and the authorised borrowing limit and operational boundary have not been exceeded.

3. CONTEXT/ BACKGROUND INFORMATION

Economic Background

3.1. The council's treasury advisors, Link Asset Services (LAS) provide their assessment of the UK and global economic landscapes, and their interest rate forecast (Appendix 3).

3.2. The Monetary Policy Committee (MPC) increased the Bank of England Base Rate from 0.50% to 0.75% in its meeting of 2 August 2018. The vote to raise was unanimous, however, the MPC signalled that the future path of interest rate rises are likely to be much more gradual than markets expect, which would be enough monetary tightening to return inflation to the 2% target over the MPCs two year horizon.

3.3. The increase in base rate has resulted in a corresponding increase in short term interest rates for both borrowing and investments; short term investment rates have increased, and the council's average investment rate is improving as maturing investments are being replaced with those at a higher interest rate. Short term borrowing rates have risen, whilst there has been little change in the longer term rates (albeit increased volatility).

3.4. The uncertainty around the terms of the withdrawal from the EU causes uncertainty for the medium and long term economic outlook. LAS's central view continues to assume that the UK will broker some kind of deal, which will result in a continuity of current market conditions into 2019/20. There are many complex and inter-related issues which make it very difficult to foresee what the impact might be on interest rates (both borrowing and investment rates) and whether there is an impact on credit and counterparty risk. Officers will be undertaking some scenario testing on the council's investment and debt portfolios between now and the 29 March 2019, taking any necessary action that is deemed appropriate to mitigate any perceived risks as a result of the outcome of the negotiations. This scenario testing will be completed in consultation with LAS.

Treasury Management Strategy

3.5. A summary of the action taken in the 6 months to September 2018 is provided in Appendix 1 to this report and further information on borrowing and investment performance is shown in the September 2018 Treasury Management statistics at Appendix 2. The main points are:

- The council entered into no of new borrowing during the period;
- The highest risk indicator during the period was 0.024% which is below the maximum benchmark of 0.050%;
- The return on investments by cash manager has exceeded the target benchmark rate;
- The return on investments by the in-house treasury team has exceeded the target benchmark rates;
- The two borrowing limits approved by full Council have not been exceeded.

3.6. Treasury management activity for the half-year has focused on a short-term horizon as summarised in the table below:

	Amount invested 1 Apr 2018 to 30 Sep 2018			
	Fixed deposits	Money market funds & Notice Accounts	Total	
Up to 1 week	-	£251.3m	£251.3m	71.5%
Between 1 week & 1 month	-	-	-	0%
Between 1 month & 3 months	£11.5m	-	£11.5m	3%
Over 3 months	£86.0m	£3.0m	£89.0m	25.5%
	£97.5m	**£254.3m**	**£351.8m**	**100%**

Summary of Treasury Activity April 2018 to September 2018

3.7 The following table summarises the treasury activity in the half year to September 2018 compared to the corresponding period in the previous year:

April to September	2017/18	2018/19
Long-term borrowing raised (General Fund)	-	-
Long-term borrowing raised (HRA)	-	-
Long-term borrowing repaid (i360)	£0.5m	£0.5m
Long-term borrowing repaid (General Fund)	-	-
Long-term borrowing repaid (HRA)	-	-
Short-term borrowing (raised)/repaid	-	-
Investments made	£305.8m	£348.8m
Investments maturing	(£275.7m)	**(£316.3)**

3.8 The Financing Costs budget has reported a total of £0.255m underspend at Month 7. The primary reason for the underspend is the an increase in investment income due to a combination of an increase in cash balances and an increase in investment rate as a result of an increase in the Bank of England Base Rate.

3.9 The following table summarises how the day-to-day cash flows in the second half-year have been funded compared to the same period in the previous year:

April - September	2017/18	2018/19
Net cash flow (shortage)/surplus	**£30.7m**	**£37.2m**
Represented by:		
Increase/(reduction) in long-term borrowing	(£0.5m)	(£0.5m)
Increase/(reduction) in short-term borrowing*	-	-
Reduction/(increase) in investments	(£30.1m)	(£32.5m)
Reduction/(increase) in bank balance	(£0.1m)	(£4.2m)

*South Downs National Park external investments

Security of Investments

3.10 A summary of investments made by the in-house team and outstanding as at 30 September 2018 in the table below shows that investments continue to be held in good quality, short term instruments. The funds invested in BBB institutions included in the table below are invested in the part-nationalised banks which are backed by Government guarantees in line with the AIS.

'AAA' rated money market funds	£27.37m	18%
'AA' rated institutions	£58.50m	37%
'A' rated institutions	£73.00m	40%
'BBB' rated institutions	£8.00m	5.%
Total	**£156.87m**	**100%**
Period – less than one week	£27.37m	18%
Period – between one week and one month	£18.00m	11%
Period – between one month and three months	£20.00m	13%
Period – between three months and 1 year	£91.50m	58%
Total	**£156.87m**	**100%**

Risk

3.11 As part of the investment strategy for 2018/19 the Council agreed a maximum risk benchmark of 0.050% i.e. there is a 99.95% probability that the council will get its investments back. The benchmark is a simple target that measures the risk based on the financial standing of counterparties and length of each investment based on historic default rates. The actual risk indicator has varied between 0.016% and 0.024% between April 2018 and September 2018. It should be remembered however that the benchmark is an 'average risk of default' measure, and does not constitute an expectation of loss against a particular investment.

3.12 In October 2017, Internal Audit undertook an audit of the treasury management function. The audit concluded that "substantial assurance" is provided on the effectiveness of the control framework operating and mitigating risks for treasury management. No recommendations were provided.

Compliance with the Annual Investment Strategy

3.13 During the reporting period, the information in this report provides assurance that the Annual Investment Strategy has been complied with in full.

Borrowing Strategy

3.14 The General Fund entered into £20.0m of planned new borrowing over the last two years. This borrowing was undertaken to reduce the council's internal borrowing position (i.e. the extent to which the council was borrowing cash from its own reserves) in light of interest rate forecasts and the reduction in certain reserves expected over the medium term.

3.15 The Housing Revenue Account (HRA) entered into a total of £14m of external borrowing and £3.2m of borrowing from the General Fund to support the 2016/17 & 2017/18 HRA Capital Programmes.

3.16 The treasury team, along with the council's treasury advisors, monitor interest rates and will seek to externalise the HRA's borrowing from the General Fund at a time which would be optimal for both the HRA and the General Fund. The Treasury Team are also exploring alternative borrowing sources, such as forward market borrowing for future capital investment plans.

3.17 The borrowing cap (or limit) on the amount of HRA borrowing permissible for capital investment was set at £156.8m for Brighton & Hove. The Minister for Housing, Communities and Local Government has recently issued a determination - Limits on Indebtedness (Revocation) Determination 2018. This came into force on 29 October 2018 and removes the HRA borrowing cap. The removal of the cap will enable the potential for substantial growth in the number of homes that can be built or purchased within the HRA. However, the HRA remain subject to the Prudential Framework, and as such all new HRA borrowing decisions will need to be affordable, prudent and sustainable and therefore will be subject to a business case. Each scheme will have to demonstrate need, value for money and affordability (that the net costs of borrowing can be met from the HRA), and the cumulative impact of new borrowing decisions on the HRA 30 Year Business Plan will be monitored and reviewed by the Chief Finance Officer. Full Council approve the Prudential Indicators which define the parameters for the council's borrowing as part of the Budget Setting process. Any expected increase in HRA borrowing will be approved as part of these indicators.

3.18 In October 2018, the treasury team, in consultation with the Council's Treasury Advisors, Link Asset Services, have been able to take advantage of an opportunity to restructure £30.0m of the council's market loan portfolio. The Royal Bank of Scotland are in the process of selling their Local Authority LOBO portfolio to an institutional investor, but were offering favourable terms to Local Authorities who wanted to repay the loans early, rather than transferring to the new lender. Repaying early and replacing with a like-for-like loan from the Public Works loans board has provided an average annual saving of £80k for the General Fund and £90k for the HRA. The borrowing has been funded initially by short term borrowing from other Local Authorities. Officers are in the process of exploring the appropriate maturity profile for replacement debt and setting trigger rates to enter into long term replacement debt in order to provide the council with an optimum outcome from the restructure.

3.19 A summary of the council's debt portfolio is summarised in Appendix 1.

Capital Strategy

3.20 The council undertakes its borrowing and investment decisions in accordance with the four statutory codes which make up the Prudential Framework. Each of these four codes has recently been updated following consultation with Local Authorities. CIPFA released revised Prudential and Treasury Management Codes in December 2017, and the Ministry for Housing, Communities and Local Government released revised Investment Guidance and MRP Guidance in February 2018.

3.21 The revisions to the Prudential Framework has introduced the requirement for Local Authorities to produce an additional report called the Capital Strategy which is to be presented and approved by members each year. The purpose of the Capital Strategy is to provide a single place for transparency and accountability of local authority non-financial investments, particularly in commercial investments such as commercial property and loans to third parties. The aim is to ensure members are fully conversant with the risks of nonfinancial investments and are aware of how the risks are proportional to the council's core service activity. The document will provide:

- An overview of the benefits and risks of all current non-financial investments;
- A summary of potential and pending non-financial investments;
- A summary of the governance arrangements for each area of non-financial investment activity, and any investment parameters where relevant;
- Some numerical analysis around non-financial investment activity in proportion to the council's revenue position, and other capital activity.

3.22 CIPFA require full compliance by 2019/20. Officers are currently working towards a fully compliant Capital Strategy for 2019/20 which will be presented alongside the budget report in February 2019.

Treasury Advisors

3.23 The council has a three year contract for treasury advisory services with Link Asset Services (LAS) to November 2018. A new contract will be awarded to Link Assets Services from an approved framework for a shorter period to December 2020. This will assist in aligning the contract end date with our Orbis partners and provide an opportunity to undertake a single procurement exercise if deemed appropriate at that time.

3.24 The council recognises that responsibility for decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers. It also recognises that there is value in employing external providers of treasury management services in order to access specialist skills and resources.

4. ANALYSIS & CONSIDERATION OF ANY ALTERNATIVE OPTIONS

4.1. This report sets out action taken in the 6 months to September 2018. Treasury management actions have been carried out within the parameters of the AIS, TMPS and Prudential Indicators. Therefore no alternative options have been considered.

5. COMMUNITY ENGAGEMENT & CONSULTATION

5.1. The council's external treasury advisors have been consulted over the content of this report. No other consultation was undertaken.

6. CONCLUSION

6.1 Treasury management is governed by a code that is recognised as "best and proper practice" under the Local Government Act 2003. The Code requires a minimum of two reports per year, one of which is required to review the previous year's performance. This report fulfils that requirement.

7. FINANCIAL & OTHER IMPLICATIONS:

Financial Implications:

7.1 The financial implications of treasury management activity are reflected in the financing costs budget set out in paragraph 3.8.

Finance Officer Consulted: James Hengeveld Date: 26/11/18

Legal Implications:

7.2 The TMSS is approved, and associated actions carried out, using powers given to the council by Part 1 of the Local Government Act 2003. These include the power for a local authority to invest for the purposes of the prudent management of its financial affairs (section 12).

7.3 Regulations made under the Local Government Act 2003 (Local Authorities (Capital Finance and Accounting) (England) Regulations 2003/3146) require local authorities to have regard to the CIPFA Code of Practice in force at the relevant time when exercising the afore-mentioned powers.

7.4 The council's policy and the actions outlined in the report, including the fact of this half yearly review, ensure compliance with the council's obligations under the Act and with relevant statutory guidance.

Lawyer Consulted: Victoria Simpson Date: 22/11/2018

Equalities, Sustainability and other significant implications:

7.5 There are no direct implications arising from this report

SUPPORTING DOCUMENTATION

Appendices:

1. A summary of the action taken in the period April 2018 to September 2018

2. September 2018 Treasury Management statistics

3. The Economy & Interest Rates – Link Asset Services

Documents in Members' Rooms

None

Background Documents

1. I. Part I of the Local Government Act 2003 and associated regulations.

2. The Treasury Management Strategy Statement, Treasury Management Practices and associated schedules 2018/19 (including the Annual Investment Strategy 2018/19) approved by Policy & Resources on 29 March 2018 and full Council on 19th April 2018.

3. Treasury Management Policy Statement 2017/18 (including Annual Investment Strategy 2017/18) – Mid-Year Review approved by Policy & Resources Committee on 30 November 2017.

4. Papers held within Financial Services, Finance & Resources Directorate.

5. The Prudential Code for Capital Finance in Local Authorities published by CIPFA 2011.