Chorley Council

Report of	Meeting	Date
Chief Executive	Governance Committee	20 September 2017

TREASURY MANAGEMENT ACTIVITY MID-YEAR REVIEW 2017/18

PURPOSE OF REPORT

1. To report on Treasury Management performance and compliance with Prudential Indicators in financial year 2017/18 to the end of July.

RECOMMENDATION(S)

2. That the report be noted.

EXECUTIVE SUMMARY OF REPORT

3. Average interest earned is 0.18% to the end of July, which is more than the target of 0.13%. As in 2016/17, cash balances have been used as a source of internal borrowing to minimise external borrowing at higher rates of interest, thereby achieving revenue budget savings.

4. Updated Capital Expenditure and Capital Financing Requirement Prudential Indicators will be presented in the Treasury Strategy report to Full Council on 27 February 2018.

5. Implementation of MiFID II from January 2018 is likely to mean that the Council will be unable to place deposits in money market funds, which may have an impact on the average rate of return achieved in future.

Confidential report Please bold as appropriate	Yes	**No**

CORPORATE PRIORITIES

6. This report relates to the following Strategic Objectives:

Involving residents in improving their local area and equality of access for all		A strong local economy	
Clean, safe and healthy communities		An ambitious council that does more to meet the needs of residents and the local area	

BACKGROUND

7. Special Council of 28 February 2017 approved the Treasury Management Policy Statement; Treasury Management Practices; Prudential Indicators for 2017/18 to 2019/20;

the Treasury Management Strategy and Treasury Indicators for 2017/18; the Annual Investment Strategy 2017/18; and the Annual Minimum Revenue Provision (MRP) Policy for 2017/18.

8. The Treasury Management Annual Report for 2016/17 was presented to Governance Committee of 21 June 2017.

9. The Code of Practice for Treasury Management requires Councils to review their treasury strategies and activities half yearly. This report satisfies that requirement.

PRUDENTIAL INDICATORS

Capital Expenditure and Capital Financing Requirement (CFR) 2017/18

10. The Prudential Indicators reported on 28 February 2017 took account of estimated capital expenditure and sources of financing from 2016/17 to 2019/20. These will be reviewed during the year, to take account of any significant changes to the capital programme and its financing as reported in budget monitoring. Revised Prudential Indicators will be presented to the budget setting Council meeting of 27 February 2018.

11. The Prudential Indicators approved for 2017/18 onwards were as follows:

Prudential Indicator 1 - Capital Expenditure

Table 1 - Capital Expenditure	**2017/18 Estimate £000**	**2018/19 Estimate £000**	**2019/20 Estimate £000**
Capital expenditure incurred directly by the Council	24,648	8,965	800
Less Capital resources			
Capital receipts	(1,215)	0	0
Grants & contributions	(11,284)	(2,312)	(370)
Revenue and reserves	(2,390)	(332)	(330)
Unfinanced amount (affects the CFR: see Prudential Indicator 2 below)	**9,759**	**6,321**	**100**
Of which:			
General capital expenditure	625	260	100
Primrose Retirement Village	331	4,836	
Market Walk Extension *	6,353		
Digital Office Park*	2,450	1,225	

* Self-financing Prudential Borrowing

Prudential Indicator 2 - Capital Financing Requirement (CFR)

Table 2 - CFR	31/3/18 Estimate £000	31/3/19 Estimate £000	31/3/20 Estimate £000
Estimated CFR at year-end	48,760	53,378	52,579
Reasons for the annual change in the CFR			
Unfinanced capital expenditure (see Table 1)	9,759	6,321	100
Annual revenue charge (MRP)	(543)	(620)	(899)
Voluntary Set Aside (Commuted Sum)		(1,083)	
Of which:			
General capital expenditure	12,650	12,521	12,241
Primrose Retirement Village	1,042	4,795	4,723
Market Walk Shopping Centre *	22,762	22,601	22,433
Market Walk Extension *	9,461	9,391	9,208
Digital Office Park*	2,845	4,070	3,974

* Self-financing Prudential Borrowing

The CFR and Borrowing 2017/18

12. The Prudential Code requires that borrowing net of investments should not exceed the CFR for the preceding year plus any anticipated increase in the current and next two years. This is in order to ensure that Councils borrow only for capital investment purposes. As at 31 March 2017, net borrowing as reported in the Treasury Management Annual Report 2016/17 was £17.582m (including £7m temporary borrowing) and therefore was well below the CFR of £39.287m at the same date. Net borrowing will not exceed the CFR in 2017/18, and the actual year-end figure will be confirmed in the Treasury Management Annual Report for the financial year.

13. As there is a large margin between net borrowing and the CFR, the Council could take additional external borrowing should it need to top-up cash balances. However, there would be a “carrying cost” of additional borrowing, because the interest rates payable would exceed the interest rates receivable on the cash balances. As indicated in Table 5 below, the average rate of interest earned this year to July is 0.18%, whereas interest payable on new PWLB loans would be 1.02% (5 years) to 2.58% (50 years) – rates as at 25 August 2017. Even though there would be a “carrying cost” of taking additional PWLB loans, this may prove necessary to achieve savings in the longer run if significant increases in interest rates on borrowing became imminent.

14. Appendix C compares this Council’s borrowing as at 30 June 2017 with that of all local authorities in England.

Operational Boundary for External Debt 2017/18

15. The Operational Boundary for external debt should reflect the most likely, but not worst-case, scenario consistent with the Council’s approved budgets. Gross borrowing and other long-term liabilities should not exceed the Operational Boundary. The figure approved on 28 February 2017 was £39.883m, being the forecast gross borrowing and other long-term liabilities as at 31 March 2018. Actual borrowing at that date is expected to be lower, because as much as possible of the CFR is matched by internal rather than external

borrowing. Use for internal borrowing is the most effective use of the Council's cash balances while available, and so far in 2017/18 no new long-term external borrowing has been taken. The Operational Boundary was set at a value based on the CFR to allow additional external borrowing should cash balances be depleted, without breaching the Prudential Indicator.

Prudential Indicator 8 The Operational Boundary for External Debt

Table 3 - Operational Boundary	31/3/18 Estimate £000	31/3/19 Estimate £000	31/3/20 Estimate £000
Borrowings	39,868	43,698	43,698
Other long-term liabilities	15	15	15
Operational boundary	**39,883**	**43,713**	**43,713**

Authorised Limit 2017/18

16. The Authorised Limit should allow headroom above the Operational Boundary to accommodate the fluctuations that can occur in cash flows. The figure approved for 2017/18 was £42.883m, and there is no reason to amend this at present.

Prudential Indicator 9 The Authorised Limit

Table 4 - Authorised Limit	31/3/18 Estimate £000	31/3/19 Estimate £000	31/3/20 Estimate £000
Borrowings	42,868	46,698	46,698
Other long-term liabilities	15	15	15
Authorised Limit	**42,883**	**46,713**	**46,713**

Ratio of Financing Costs to the Revenue Stream 2017/18

17. The Ratio of Financing Costs to the Revenue Stream shows the percentage of the Council's income from Government grants and council tax that has been used to meet interest costs and debt repayment. The actual figure for 2017/18 will be presented in the Treasury Management Annual Report 2017/18 in June 2018.

Incremental Impact of Capital Investment Decisions 2017/18

18. The Incremental Impact of Capital Investment Decisions measures the cumulative impact of capital expenditure on the revenue budget. It is not possible to make a meaningful comparison against this indicator other than when it is restated in the annual Treasury Strategy, which will be presented to Council in February 2018.

TREASURY ACTIVITY

19. Investment activity up to the end of July 2017 is summarised in the following table.

Table 5 - Investment Activity	Average Daily Investment £000	Earnings to 31 July 2017 £	Average Rate %
Fixed Term Deposits	-	-	-
Call Accounts	852	318	0.11
Money Market Funds	3,175	2,085	0.20
Total	**4,027**	**2,403**	**0.18**

Compared to 2016/17, the main change has been the lower balance available to invest, which means that it has not been possible to invest for longer periods in order to achieve higher interest rates.

A full list of investments as at 31 July 2017 is shown below.

Table 6 - Investments as at 31 July 2017				
Counterparty	**Type**	**Amount £**	**Invested date**	**Maturity date**
Standard Life	MMF	3,000,000	Various	On call
Barclays	Call account	1,004,406	Various	On call
Total		**4,004,406**		

There are no changes proposed to the current list of Financial Institutions and Investment Criteria.

20. The average interest earned of 0.18% exceeds the target of 0.13% (being the average LIBID 7-day rate plus 15%). However, to date the average interest earned has not exceeded the Capita suggested earnings rate of 0.25% for 2017/18 (see Table 7 below). This is because the Capita rate is based on 3-month term deposits, whereas this council's deposits have been placed only in call accounts and money market funds.

21. Appendix C compares this Council's investments as at 30 June 2017 with the total for all local authorities in England.

TREASURY CONSULTANTS' ADVICE

22. Appendix A presents the advice of Capita Asset Services and their economic research consultants Capital Economics in respect of economic matters in the first quarter of 2017/18. In addition, a detailed commentary on interest rate forecasts is presented as Appendix B. Bank rate and PWLB borrowing rate forecasts are given from September quarter 2017 through to March quarter 2020.

23. An increase in Bank Rate from 0.25% to 0.50% is still expected in the June quarter of 2019. So far the Bank Rate forecast remains unchanged from that included in the Treasury Strategy for 2017/18.

24. Capita's suggested budgeted investment earning rates for investments up to about three months duration in each financial year for the next seven years are as follows:

Table 7 - Average Earnings in each financial year		
	Revised August 2017	Original February 2017
2017/18	0.25%	0.25%
2018/19	0.25%	0.25%
2019/20	0.50%	0.50%
2020/21	0.75%	0.75%
2021/22	1.00%	1.00%
2022/23	1.50%	1.50%
2023/24	1.75%	1.75%
Later years	2.75%	2.75%

25. The most recent estimate is compared to the estimated earnings rate available at the time the Treasury Management Strategy was presented for approval in February 2017. The suggested earnings rates are unchanged so far this financial year.

26. Compared to the previous interest rates forecast, PWLB borrowing rates are currently a little lower than expected. Gradually increases through to March quarter of 2020 are still forecast. Should rates begin to increase more steeply, it may become advisable to take additional borrowing sooner rather than later to achieve longer term savings.

MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE (MiFID) II

27. Appendix D presents an update on the implementation of MiFID II in the United Kingdom. In brief, to continue using regulated products such as money market funds Chorley Council would have to opt-up to Professional Client status. The likelihood is that the Council would fail the minimum financial instrument portfolio size test of £10m and therefore would not be able to use MMFs from January 2018.

28. This would increase the likelihood of having to deposit cash in the Debt Management Office’s Debt Management Account Deposit Facility at a low rate of interest (currently 0.10%), but with a high degree of security. Other local authorities might offer a slightly higher rate of interest than the DMO for short-term deposits, but there is no certainty of finding a council which requires cash at the same time that this Council needs to invest funds temporarily.

CIPFA CONSULTATIONS ON THE TREASURY MANAGEMENT CODE AND PRUDENTIAL CODE

29. A summary of the proposed changes to CIPFA’s Treasury Management Code and Prudential Code is presented as Appendix E. Several of the proposed changes are

inevitably of a technical nature, and those incorporated into the Codes will be explained when implemented.

30. It is clear that some of the changes are intended to address concerns expressed in the media in recent months about the extent to which local authorities have been incurring capital expenditure on income-generating properties to meet budget shortfalls following cuts in government funding. The changes to the Prudential Code should not affect this Council's existing capital expenditure plans, though there would be a specific requirement to report on risks associated with the capital strategy.

CIPFA CONSULTATION ON ADOPTION OF IFRS 9 FINANCIAL INSTRUMENTS IN CODE OF PRACTICE ON LOCAL AUTHORITY ACCOUNTING IN THE UNITED KINGDOM 2018/19

31. The CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 will adopt the IFRS 9 accounting rules for Financial Instruments. The changes could have an impact on councils which invest in companies, or place deposits in enhanced money market funds.

32. Any investments which would be accounted for as "available for sale" at present would move into the "fair value through profit or loss" category. This would mean that gains or losses from changes in the fair value of financial assets would be reflected in the surpluses or deficits in the Provision of Services in local authorities' accounts, rather than being held in a reserve until realised on sale of the assets. It is not clear whether the DCLG will introduce a statutory override to reverse the impact of the gains or losses.

33. At present the proposed change would not affect this Council, though it may be desirable to delete enhanced MMFs from the investment counterparties list in the Treasury Strategy for 2018/19 onwards.

IMPLICATIONS OF REPORT

34. This report has implications in the following areas and the relevant Directors' comments are included:

Finance	✓	Customer Services	
Human Resources		Equality and Diversity	
Legal		Integrated Impact Assessment required?	
No significant implications in this area		Policy and Communications	

COMMENTS OF THE STATUTORY FINANCE OFFICER

35. This report complies with statutory requirements. Statistical content is consistent with the assumptions in the approved capital and revenue budgets for 2017/18.

COMMENTS OF THE MONITORING OFFICER

36. The Monitoring Officer has no comments.

GARY HALL
CHIEF EXECUTIVE

There are no background papers to this report.

Report Author	Ext	Date	Doc ID
Michael Jackson	5490	29 August 2017	Treasury Management Activity Mid-Year Review 2017-18.docx