

<b>Report to:</b>	Audit and Governance Committee	<b>Date of Meeting:</b>	6 December 2017
	Cabinet		7 December 2017
	Council		25 January 2018
<b>Subject:</b>	Revenue and Capital Budget Update - Treasury Management Position to October 2017		
<b>Report of:</b>	Head of Corporate Resources	<b>Wards Affected:</b>	All wards
<b>Portfolio:</b>	Cabinet Member - Regulatory, Compliance and Corporate Services		
<b>Is this a Key Decision:</b>	Yes	<b>Included in Forward Plan:</b>	Yes
<b>Exempt / Confidential Report:</b>	No		

### Summary:

This report provides Members with a review of the Treasury Management activities undertaken to 31<sup>st</sup> October 2017. Cabinet receives this mid-year review to allow monitoring against the Treasury Management Policy and Strategy statement approved by Cabinet and Council in March 2017. This report is also the second of the ongoing quarterly monitoring reports provided to Audit & Governance Committee, whose role it is to carry out scrutiny of treasury management policies and practices.

### Recommendation(s):

Members are requested to note the Treasury Management update to 31<sup>st</sup> October 2017, to review the effects of decisions taken in pursuit of the Treasury Management Strategy and to consider the implications of changes resulting from regulatory, economic and market factors affecting the Council's treasury management activities.

### Reasons for the Recommendation(s):

To ensure that Members are fully appraised of the treasury activity undertaken to 31<sup>st</sup> October 2017 and to meet the reporting requirements set out in Sefton's Treasury Management Practices and those recommended by the CIPFA code.

### Alternative Options Considered and Rejected: (including any Risk Implications)

N/A

## What will it cost and how will it be financed?

### (A) Revenue Costs

The financial position on the external investment budget to the end of October indicates a shortfall of £14k compared to the proportion of the budget to date. If current market conditions prevail an under-recovery of around £25k will be experienced. The Head of Corporate Resources and Head of Regulation and Compliance have been consulted.

### (B) Capital Costs

None.

## Implications of the Proposals:

<b>Resource Implications (Financial, IT, Staffing and Assets):</b> Under-recovery on Debt Repayment/Net Interest Budget.
<b>Legal Implications:</b> The Council has a statutory duty to review its Treasury Management activities from time to time during the financial year.
<b>Equality Implications:</b>  None.

## Contribution to the Council's Core Purpose:

Protect the most vulnerable: n/a
Facilitate confident and resilient communities: n/a
Commission, broker and provide core services: n/a
Place – leadership and influencer: Support strategic planning and promote innovative, affordable and sustainable capital investment projects through application of the CIPFA Prudential Code.
Drivers of change and reform: The Treasury Management function ensures that cash flow is adequately planned and cash is available when needed by the Council for improvements to the borough through its service provision and the Capital Programme.
Facilitate sustainable economic prosperity: Pursuit of optimum performance on investments activities and minimising the cost of borrowing and the effective management of the associated risk continues to contribute to a balanced budget for the Council.
Greater income for social investment: n/a
Cleaner Greener: n/a

## What consultations have taken place on the proposals and when?

### (A) Internal Consultations

The Head of Corporate Resources (FD 4930/17) and Head of Regulation and Compliance (LD 4215/17) have been consulted and any comments have been incorporated into the report.

### (B) External Consultations

None.

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### Appendices:

There are no appendices to this report

### Background Papers:

There are no background papers available for inspection.

## 1. Background to the Report

- 1.1. As recommended under CIPFA's revised 2001 Code of Practice on Treasury Management in Public Services, the Council's Treasury Management Policy and Strategy document for 2017/18 (approved by Council on 2<sup>nd</sup> March 2017) included a requirement for regular updates to be provided on the investment activity of the Authority. This report is the second of such reports for the year and presents relevant Treasury Management information for the period ending 31<sup>st</sup> October 2017.
- 1.2. The report includes information on the investments held / entered into during the period and the interest rates obtained (with a comparison of performance against a standard benchmark figure). In addition, the report highlights whether there has been any variance from the Treasury Management Policy Strategy and the Council's approved Prudential Indicators (the operational boundaries within which the Council aims to work).

## 2. Investments Held

- 2.1. Investments held at the 31/10/2017 comprise the following:

<b>Overnight Deposits</b>					
<b>Institution</b>	<b>Deposit</b>	<b>Rate</b>	<b>Maturity</b>	<b>On Current Counterparty List?</b>	<b>Rating</b>
	<b>£m</b>	<b>%</b>			
Svenska Handelsbanken	3.000	0.20	n/a	Yes	AA-

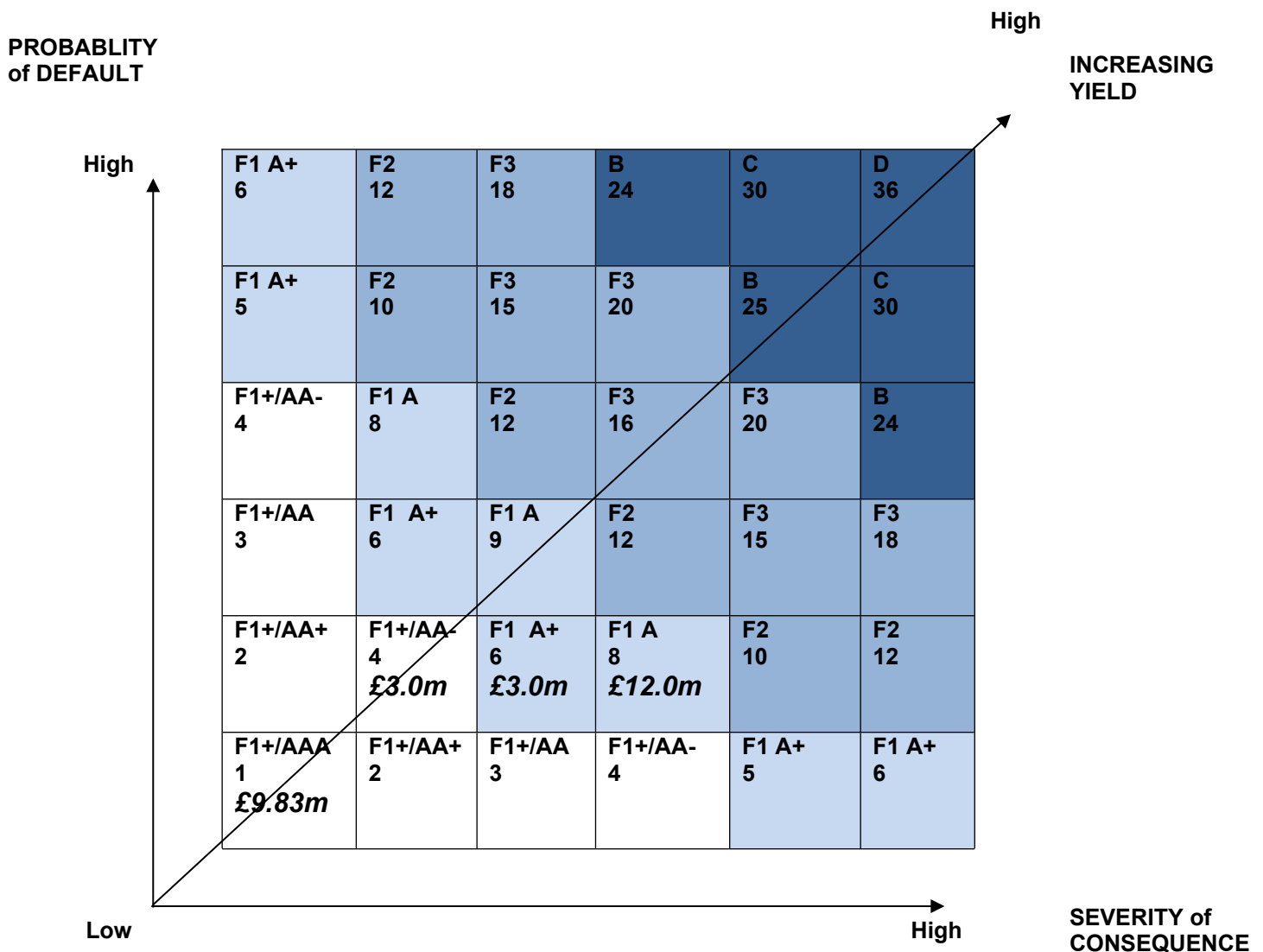
BNP Paribas	3.210	0.22	n/a	Yes	AAA
Invesco	0.920	0.19	n/a	Yes	AAA
Federated Investors	3.280	0.21	n/a	Yes	AAA
Insight	1.290	0.21	n/a	Yes	AAA
Standard Life	1.130	0.20	n/a	Yes	AAA
Total	12.830				
<b>Call Accounts</b>					
Santander	2.000	0.40	95 day notice	Yes	A
Santander	1.000	0.45	120 day notice	Yes	A
Bank of Scotland	3.000	0.60	175 day notice	Yes	A+
Goldman-Sachs	3.000	0.75	185 day notice	Yes	A
Total	9.000				
<b>Fixed Term Deposits</b>					
Nationwide	3.000	0.37	17/11/2017	Yes	A
C'wealth Bank of Australia	3.000	0.45	19/02/2018	Yes	A
Total	6.000				
<b>Other</b>					
CCLA	5.000	5.31	n/a	Yes	n/a
Total	5.000				
<b>Total Investments</b>	<b>32.830</b>				

- 2.2. The above cash balances represent the full range of earmarked reserves such as school's balances.
- 2.3. All of the investments made since April 2017 have been with organisations on the current counterparty list. The maximum level of investment permitted in the Treasury Management Strategy in any one institution, or banking group, is currently £25m. Whilst the maximum should be retained, in case economic conditions change, a day to day operational maximum of 10% of the total portfolio is currently being imposed. This will spread the risk of investments for the Council, but will have a small detrimental impact on the returns the Council will receive in the future. The Council has remained within that boundary during the year. At present, it is not expected that there will be any need to review this limit.
- 2.4. The Council will only invest in institutions that hold a minimum Fitch rating of A- for banking institutions, or AAA for money market funds. The ratings applied to investment grade institutions, and the much riskier speculative grade institutions, as defined by Fitch, have been placed into a risk matrix (paragraph 2.5).
- 2.5. An investment has been made with the Church, Charities and Local Authority Investment Fund (CCLA) in June 2014. CCLA invest in commercial property which is rented out to enterprises as retail units, warehousing, and offices. The majority of properties owned are in the south of the country where the market is

currently more buoyant than the north. The Council has in effect bought a share of the property portfolio, and returns paid are in the region of 5%. This is seen as a long term investment with the potential for capital growth of the investment as property prices potentially increase. However, when the investment is made fees are deducted from the initial investment hence in the first year any income received covers these fees.

2.6. The Net Asset Value of the Property Fund has increased from 287.77p per unit to 294.60p per unit between April and September 2017, an increase of 2.4% in the value of the Council's investment. The rate of inflation (CPI) to the end of September was 3.0% by comparison hence the value of the investment is being marginally depleted with income received at 5% representing a real return.

2.7. The matrix below shows how the Council has set its risk appetite by being risk averse and putting security and liquidity before yield:



SEFTON RISK TOLERANCE

INVESTED

LOW RISK

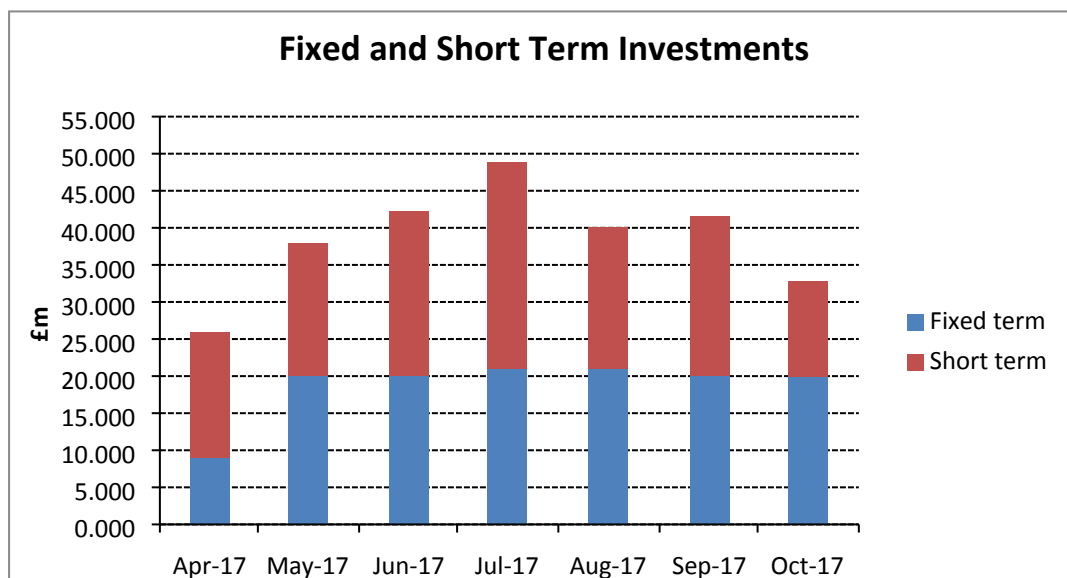
1 - 4

Investment Grade

£12.83m

LOW - MEDIUM RISK	5 - 9	Investment Grade	£15.00m
MEDIUM RISK	10 - 20	Investment Grade	Nil
HIGH RISK	21 - 36	Speculative Grade	Nil

2.8. The ratio of overnight deposits (short term) to fixed term investments is shown below:



2.9. No new fixed term investments have been made since the last quarter. A deposit of £1m that was placed with Lloyds in a 32 day notice account in July has now matured but was not reinvested. A call was placed on £1m held in a 120 day notice account with Santander to be returned at the end of February 2018.

2.10. Sector, our Treasury Advisors, have supplied the interest rate forecast below:

Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019
0.50%	0.50%	0.50%	0.50%	0.75%	0.75%	0.75%	0.75%

*"The overall balance of risks to economic recovery in the UK is currently to the downside but huge variables over the coming few years include just what final form Brexit will take, when finally agreed with the EU, and when.*

*We remain in a very difficult investment environment. Whilst counterparty risk appears to have eased, market sentiment has still been subject to bouts of, sometimes, extreme volatility and economic forecasts abound with uncertainty.*

*Short term interest rates rose to reflect the rate hike but longer dated rates were pared back on the weaker outlook for further hikes. Political uncertainty and Brexit negotiations are likely to continue to weigh on the economy. With Sterling giving up some pre-hike gains, imported inflation is likely to be a feature for some time, which, along with increased mortgage payments, will keep pressure on household budgets and potentially dampen sentiment."*

2.11. The Council will continue to maximise any investment opportunities as they arise, but in light of the current cash flow forecast it is not envisaged that any substantial increase in returns can be achieved for the remainder of the current financial year as cash balances available for investment are forecast to be low.

### 3. Interest Earned

3.1. The actual performance of investments against the profiled budget to the end of October 2017 and the forecast performance of investments against total budget at year end is shown below:

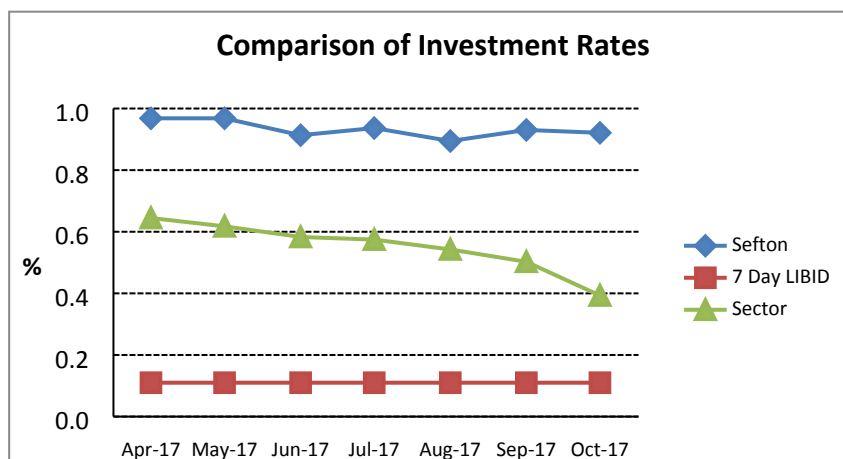
	<b>Profiled Budget £m</b>	<b>Actual £m</b>	<b>Variance £m</b>
<b>Oct-17</b>	0.236	0.222	0.014

	<b>Total Budget £m</b>	<b>Forecast Out-turn £m</b>	<b>Variance £m</b>
<b>2017/18</b>	0.375	0.350	0.025

3.2. The budgeted investment return for the financial year 2017/18 was set at £0.375m on 1<sup>st</sup> April 2017. The investment return by the end of the financial year is currently forecast to be £0.350m. The under recovery of £25k and the variance of £14k to the end of October can be explained by declining investment rates during the first half of 2017/18 under the economic conditions described in 2.9 above.

3.3. There has been some minor improvement in investment rates since the Bank of England base rate increase was announced in early November. As mentioned in paragraph 2.10 it is not envisaged that improved rates can be taken advantage of before the end of the financial year.

3.4. The Council has achieved an average rate of return on its investments that has out-performed the 7 day LIBID and the model portfolio provided by Sector:



- 3.5. Sefton has recently joined a regional Treasury Management working group for the purposes of sharing professional advice and experience. At the meeting of 28<sup>th</sup> September, Sefton proposed the sharing of investment information so that our returns can be compared with those of neighbouring authorities. The group agreed that this would be beneficial and initial work to collect the required data should be undertaken with Rochdale taking the lead. It is anticipated that benchmarking will be implemented for 2017/18 year-end reporting.

#### **4. Markets in Financial Instruments Directive (MiFID II)**

- 4.1. From 3<sup>rd</sup> January 2018 the Financial Conduct Authority will be obliged to treat all Local Authorities as “retail clients” under European Union legislation (MiFID II). The client status of the Local Authority relates to its knowledge and experience with regards to the use of regulated investment products and the decision-making processes it has in place for making such investments. The directive is focused on products such as Certificates of Deposit, Gilts, Corporate Bonds and investment funds, including Money Market Funds.
- 4.2. Sefton Council utilises several Money Market Funds for its short term investments. The Council will need to opt up to “professional status” in order to continue to have access to these funds as an investment option as they are not available to retail clients.
- 4.3. A number of applications have now been submitted with supporting evidence in order to secure professional status before the deadline. It is anticipated that the applications will be successful and there will be no requirement to alter investment activity as Sefton’s knowledge, experience and investment processes are of a standard that will allow professional status. Alternative investment products such as reserve accounts with the major banks remain available as a contingency.

#### **5. Revised CIPFA Codes**

- 5.1. CIPFA is currently conducting an exercise to consult local authorities on revising the Treasury Management Code and Cross Sectoral Guidance Notes, and the Prudential Code. CIPFA is aiming to issue the revised codes during November and this will impact the 2018/19 Treasury Management Policy and Strategy.
- 5.2. Officers are monitoring developments and will report to members when the new codes have been agreed and issued and on the likely impact. Any significant changes will be considered at the next update.

#### **6. Prudential Indicator Monitoring**

- 6.1. Prudential indicators are an integral component of measuring how prudently a Council is acting with regard to its finances. They were introduced into all local authorities (by CIPFA) following the Local Government Act 2003. A number of measures/limits/parameters including capital financing, external debt, impact on council tax, and treasury management are set prior to the start of the year and are monitored on a quarterly basis.



6.2. As at the end of September 2017 (Q2) none of the prudential indicators had been breached.

## **7. Capital Financing Strategy**

7.1. The Council is currently internally borrowed. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as an alternative measure. This strategy is prudent as investment returns remain low whilst reducing the Council's cost of borrowing. This position also reduces counterparty risk.

7.2. Due to the timing of grant income and revenues received during the financial year the profile of the Council's cash balances is front loaded. External borrowing in the short term may be required to maintain the Council's cash flow during March 2018 when it is forecast that £5m of borrowing may be required. Short term borrowing from another Local Authority with current offer rates at 0.55% over a 3 month period would incur an estimated £7k in additional loan charges.

7.3. Officers will continue to monitor the cash flow and report to members by the end of next quarter regarding any requirement for additional borrowing in March 2018.

7.4. The potential requirement for borrowing in 2018/19 will be assessed once the 2018/19 cash flow is finalised. The timing of any borrowing needs to be mindful of the current position of the Bank of England regarding future interest rate rises and its impact upon the Medium Term Financial Plan, and advice will be taken from Sector. The positive effect upon investment income received will also need to be assessed.