AUDIT AND GOVERNANCE COMMITTEE – 19 SEPTEMBER 2018

24. REVENUE AND CAPITAL BUDGET UPDATE - TREASURY MANAGEMENT POSITION TO JULY 2018

The Committee considered the report of the Head of Corporate Resources which provided a review of the Treasury Management activities undertaken to 31 July 2018. This was the first of the ongoing quarterly monitoring reports provided to the Audit and Governance Committee whose role it is to carry out scrutiny of treasury management policies and practices.

The Service Manager, Treasury and Capital presented the report and answered questions thereon.

RESOLVED: That

(1) the Treasury Management update to 31 July 2018 be noted; and

(2) the effects of decisions taken in pursuit of Treasury Management Strategy and the implications of changes resulting from regulatory, economic and market factors affecting the Council's treasury management activities, be noted.

Report to:	Audit and Governance Committee	Date of Meeting:	Wednesday 19 September 2018
Subject:	Treasury Management Position to July 2018		
Report of:	Head of Corporate Resources	Wards Affected:	All Wards
Portfolio:	Cabinet Member - Regulatory, Compliance and Corporate Services		
Is this a Key Decision:	No	Included in Forward Plan:	No
Exempt / Confidential Report:	No		

Summary:

This report provides Members with a review of the Treasury Management activities undertaken to 31st July 2018. Further monitoring reports will be presented to Audit & Governance Members on a quarterly basis, 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 31st July 2018, 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 31st July 2018 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 July indicates a nil variance to the end of the period. The forecast to the end of the financial year is also on target.

(B) Capital Costs

None.

Implications of the Proposals:

Resource Implications (Financial, IT, Staffing and Assets): None - External Interest forecast is on target.
Legal Implications: The Council has a statutory duty to review its Treasury Management activities from time to time during the financial year.
Equality Implications: 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 5272/18) and Head of Regulation and Compliance (LD 4496/18) have been consulted and any comments have been incorporated into the report.

(B) External Consultations

N/A

Implementation Date for the Decision

With immediate effect.

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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 2017 Code of Practice on Treasury Management in Public Services, the Council's Treasury Management Policy and Strategy document for 2018/19 (approved by Council on 1st March 2018) included a requirement for regular updates to be provided on the investment activity of the Authority. This report is the first of such reports for the year and presents relevant Treasury Management information for the period ending 31st July 2018.

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 and 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 31/07/2018 comprise the following:

Institution		Deposit £m	Rate %	Maturity	Rating
Money Market Funds					
Aviva		4.230	0.53	n/a	AAA
BNP Paribas		4.230	0.53	n/a	AAA
Goldman Sachs		0.850	0.50	n/a	AAA
Invesco		4.230	0.53	n/a	AAA
Federated Investors		3.920	0.55	n/a	AAA
Insight		3.920	0.51	n/a	AAA
Standard Life		3.920	0.55	n/a	AAA
	Total	25.300			
Call Accounts					
Santander		3.000	0.70	95 day notice	A
GSIB		3.000	0.82	185 day notice	A
	Total	6.000			
Fixed Term Deposits					
Lloyds		3.000	0.75	16/11/2018	A+
ANZ		3.000	0.72	30/11/2018	AA-
	Total	6.000			
Property Fund					
CCLA		5.000	4.47	n/a	n/a
	Total	5.000			
TOTAL INVESTMENTS		42.300			

2.2. The above cash balances represent the full range of earmarked reserves such as school's balances.

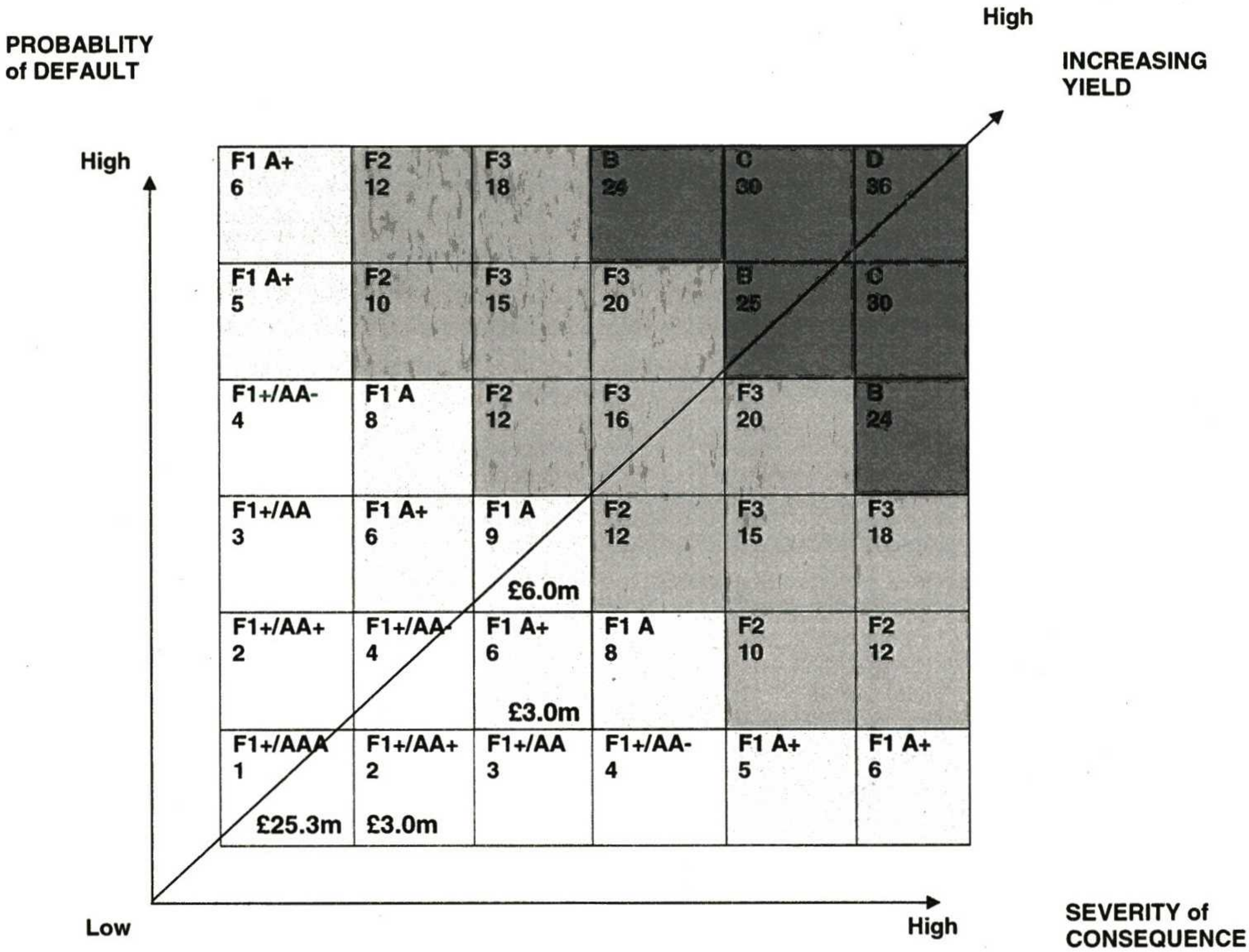
2.3. All of the investments made since April 2018 have been with organisations on the current counterparty list. The maximum level of investment permitted in the Treasury Management Strategy in any one institution, or banking group, is currently £25m. Whilst the maximum should be retained, in case economic 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 2.7).

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 4%. This is a long-term investment with the potential for capital growth of the investment as property prices potentially increase.

2.6. The Net Asset Value of the Property Fund has increased from 291.21p per unit to 303.61p per unit over a 12-month period to June 2018, an increase of 4.1% in the value of the Council's investment. The rate of inflation (CPI) to the end of June was 2.4% by comparison hence the value of the investment is being marginally increased with income received at 4.47% 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	1 - 4	Investment Grade	£28.3m
LOW – MEDIUM	5 - 9	Investment Grade	£9.0m
MEDIUM	10 - 20	Investment Grade	Nil
HIGH	21 - 36	Speculative Grade	Nil

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

2.9. Two fixed term investments of £3m have been made during May 2018, one with Lloyds Bank and one with Australia and New Zealand Bank. Two amounts of £3m have also been placed in call accounts with Santander and Goldman Sachs International Bank.

2.10. The Council will continue to maximise any investment opportunities as they arise, but considering the current cash flow forecast it is not envisaged that any significant 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 July 2018 and the forecast performance of investments against total budget at year end is shown below:

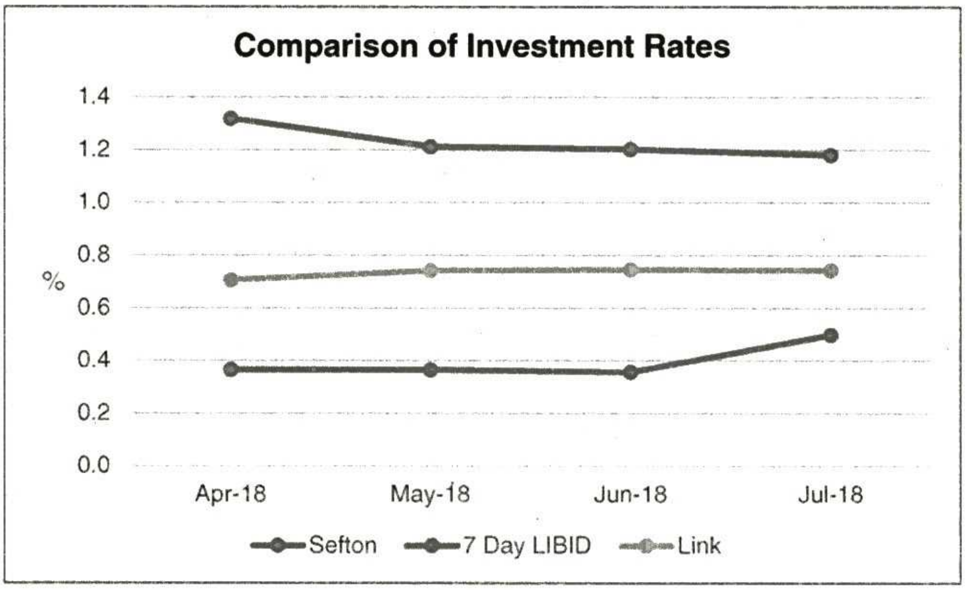
	Profiled Budget £m	Actual £m	Variance £m
Jul-18	0.137	0.137	0.000

	Total Budget £m	Forecast Out-turn £m	Variance £m
2018/19	0.375	0.375	0.000

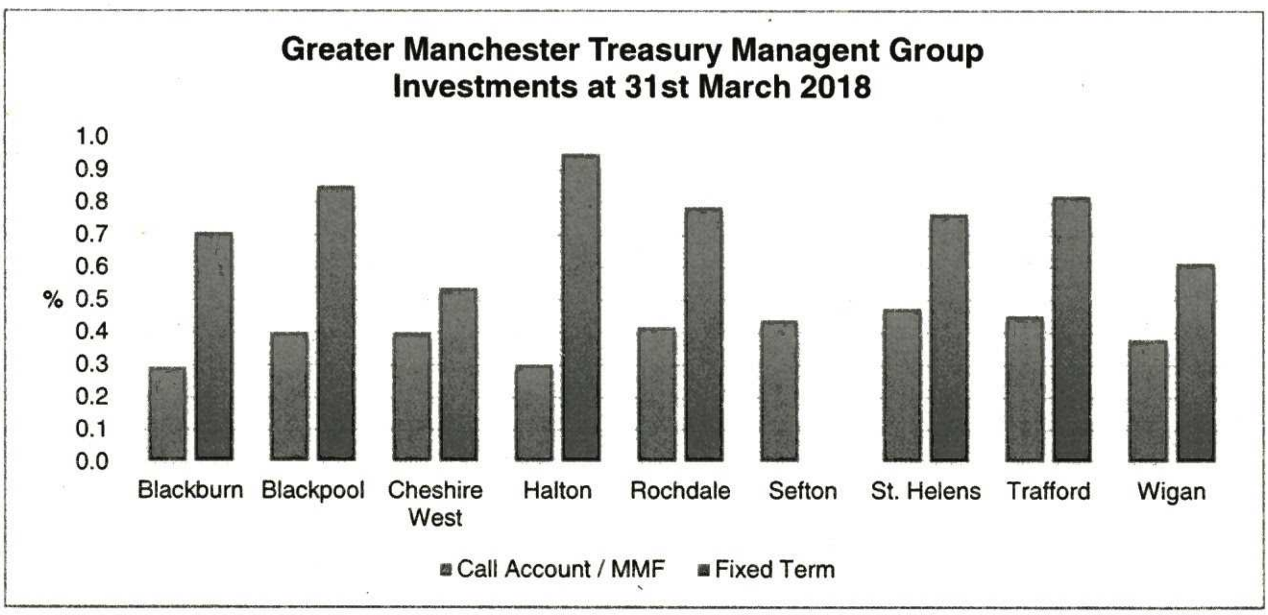
3.2. The budgeted investment return for the financial year 2018/19 was set at £0.375m on 1st April 2018. The actual investment return to the end July was on target and the forecast to year end is also a nil variance to budget.

3.3. There has been some improvement in investment rates since the Bank of England base rate increase was announced on 2nd August. 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 Link:



3.5. Sefton has joined a regional Treasury Management working group for the purposes of sharing professional advice and experience. The group has shared the following benchmarking information to the end of March 2018:



3.6. Sefton's return on Money Market Funds (0.44%) was higher than the majority of average rates achieved across the group to the end of March 2018.

3.7. There were no fixed term investments held at that date however, hence a comparison cannot be made with the other local authorities for this type of deposit.

3.8. To successfully manage liquidity risk, Sefton's policy is to maintain a minimum of £10m of its investment portfolio available for immediate use. These funds are held in Money Market Funds or deposit accounts with instant access. Due to the timing of grant payments and revenues, and Sefton's internally borrowed position, balances at the end of March 2018 were at a reduced level. Holding fixed term investments at that time was therefore, not considered prudent, and funds remained in instant access accounts until the position changed.

3.9. As shown in paragraph 2.1 (above), Sefton has now opted to place fixed term deposits at rates of between 0.72% and 0.75% in May 2018 (see table 2.1 above) as grant payments and revenues have now increased balances sufficiently during April and May 2018 to allow cash to be invested over longer periods.

4. Interest Rate Forecast

4.1. Link Asset Services, our Treasury Advisors, have supplied the interest rate forecast below:

	Sep18	Dec18	Mar19	Jun19	Sep19	Dec19	Mar20	Jun20	Sep20	Dec20	Mar21
Bank Rate	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.50%	1.50%
5yr PWLB	2.00%	2.00%	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%	2.60%
10yr PWLB	2.40%	2.50%	2.50%	2.60%	2.70%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%
25yr PWLB	2.80%	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%	3.50%	3.50%
50yr PWLB	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%

We do not think that the MPC will increase the Bank Rate in February 2019, ahead of the deadline in March for Brexit. We also feel that the MPC is more likely to wait until August 2019, than May 2019, before the next increase, to be followed by the next increases in May and November 2020 to reach 1.5%.

However, and this is a VERY BIG caveat, the forecasts above by the MPC and ourselves are predicated on an assumption that sufficient progress is made, in respect of negotiations, to produce a reasonable agreement for Brexit that benefits both the EU and the UK in a sensible manner. If no agreement is reached at all, then our forecasts for increases in Bank rate and PWLB rates will be subject to greater change, most likely downwards.

(Link Asset Services, 07.08.2018)

5. Markets in Financial Instruments Directive (MiFID II)

5.1. From 3rd January 2018, the Financial Conduct Authority is obligated 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.

5.2. As at 31st July 2018 the Council has opted up to "professional status" with the following institutions to continue to have access to these funds as an investment option as they are not available to retail clients:

Money Market Funds

- Aberdeen
- Amundi
- Aviva
- BNP Paribas
- Goldman Sachs
- Invesco
- Morgan Stanley
- Federated Investors
- Insight
- Standard Life

Banks

- Australia and New Zealand Banking Group
- Commonwealth Bank of Australia
- Goldman Sachs International Bank
- Toronto Dominion Bank

Building Societies

- Coventry
- Leeds

Property Funds

- CCLA

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 June 2018 (Q1) the Prudential Indicators for Capital Expenditure and the Capital Financing Requirement have been exceeded:

	Original Estimate 2018/19 £m	Estimate Jun-18 £m	Variance £m
Capital Expenditure	31.010	40.460	9.450
Capital Financing Requirement	236.571	238.193	1.622

6.3. The increase in estimated capital expenditure for 2018/19 has resulted from an underspend on the 2017/18 Capital Programme and slippage of proposed spending into 2018/19 financial year. The main areas of underspend and the principle reasons for the carry forward are:

- Schools and Families £2.235m – a proposed scheme at Litherland Moss was put on hold due to the school potentially becoming an Academy. Funding will be approved and redistributed to other school's schemes in 2018/19.
- Locality Services Provision £1.913m – Council transformation has meant that part of the vehicle replacement programme was put on hold until the reorganisation to the new Green Sefton service was completed.
- Locality Services Commissioned £1.822m – road schemes which are dependent on weather conditions were delayed during 2017/18.
- Communities £1.776m – as mentioned above, transformation to the Green Sefton service has meant that several projects were put on hold whilst the reorganisation was completed.
- Older People £1.478m – the majority of slippage related to the Disabled Facilities Grant which is to be utilised on wider social care projects as per the grant conditions. Further consideration is to be given to these projects in 2018/19.

6.4. The Capital Financing Requirement has increased to a lesser degree as the majority of the additional expenditure will be funded from Grants and Contributions rather than new borrowing.

6.5. A report will be submitted to Cabinet and Council to advise of the variance and to seek approval to set revised Prudential Indicators for Capital Expenditure and the Capital Financing Requirement for 2018/19.