POLICY & RESOURCES COMMITTEE	Agenda Item 78 Brighton & Hove City Council

Subject:		**Treasury Management Strategy Statement 2019/20 - Mid Year Review**	
Date of Meeting:		**5 December 2019**	
Report of:		**Executive Director for Finance & Resources**	
Contact Officer:	**Name:**	**James Hengeveld** **Haley Woollard**	**Tel: 01273 291242** **Tel: 01273 291246**
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Ward(s) affected:		**(All Wards);**	

FOR GENERAL RELEASE

1. PURPOSE OF REPORT AND POLICY CONTEXT

1.1 The 2019/20 Treasury Management Strategy Statement (TMSS), practices and schedules were approved by Policy, Resources & Growth Committee on 14 February 2019 and full Council on 28 February 2019.

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 2019/20.

2. RECOMMENDATIONS:

That the Policy & Resources Committee:

2.1 Notes the key actions taken during the first half of 2019/20 to meet the TMSS and the investment strategy as set out in this report.

2.2 Notes the reported compliance with the AIS for the period under review.

2.3 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. This is included at Appendix 2.

3.2. The first half of 2019/20 has seen UK economic growth fall as a result of Brexit uncertainty, and the wider impact of global growth concerns. In its Inflation Report of 1 August, the Bank of England expressed concern about the outlook for both the UK and major world economies. The Monetary Policy Committee (MPC) meeting of 19 September reemphasised their concern about the downturn in world growth and also expressed concern that prolonged Brexit uncertainty would contribute to a build-up of spare capacity in the UK economy, especially in the context of a downturn in world growth. This mirrored investor concerns around the world which are now expecting a significant downturn or possibly even a recession in some major developed economies. It was therefore no surprise that the MPC has so far left the Bank Rate unchanged at 0.75% throughout 2019 and is expected to hold off on changes until there is some clarity on what is going to happen over Brexit.

Treasury Management Strategy

3.3. A summary of the action taken in the 6 months to September 2019 is provided in Appendix 1 to this report and further information on borrowing and investment performance is shown in the September 2019 Treasury Management statistics at Appendix 2. The main points are:

- The council entered into £10.000m of new borrowing during the period;
- The highest risk indicator during the period was 0.023% which is below the maximum benchmark of 0.050%;
- 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.

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

	Amount invested 1 Apr 2019 to 30 Sep 2019			
	Fixed deposits	Money market funds & Notice Accounts	Total	
Up to 1 week	-	£274.3m	£274.3m	73.7%
Between 1 week & 1 month	£5.0m	-	£5.0m	1.3%
Between 1 month & 3 months	£30.0m	-	£30.0m	8.1%
Over 3 months	£58.0m	£5.0m	£63.0m	16.9%
	£93.0m	**£279.3m**	**£372.3m**	**100.0%**

Summary of Treasury Activity April 2019 to September 2019

3.6 The following table summarises the treasury activity in the half year to September 2019 compared to the corresponding period in the previous year:

April to September	2018/19	2018/19
Long-term borrowing raised (General Fund)	-	(£7.5m)
Long-term borrowing raised (HRA)	-	(£2.5m)
Long-term borrowing repaid (i360)	£0.5m	£0.5m
Long-term borrowing repaid (General Fund)	-	£0.3m

Long-term borrowing repaid (HRA)	-	£0.4m
Short-term borrowing (raised)/repaid	-	£8.0m
Investments made	£348.8m	£372.3m
Investments maturing	(£316.3m)	(£378.1m)

3.7 In 2018/19, £290k was set aside in the Financing Costs earmarked reserves to fund potential net financing cost pressures in 2019/20. At TBM7, it is forecast that £230k of this will be drawn down to support the Financing Cost budget in the year.

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

April to September	2018/19	2019/20
Net cash flow (shortage)/surplus	**£37.2m**	**(£5.3m)**
Represented by:		
Increase/(reduction) in long-term borrowing	(£0.5m)	£8.1m
Increase/(reduction) in short-term borrowing*	-	(£8.0m)
Reduction/(increase) in investments	(£32.5m)	£5.8m
Reduction/(increase) in bank balance	(£4.2m)	(£0.6m)

*including South Downs National Park external investments

Security of Investments

3.9 A summary of investments made by the in-house team and outstanding as at 30 September 2019 in the table below shows that investments continue to be held in good quality, short term instruments.

'AAA' rated money market funds	£84.00m	46.3%
'AA' rated institutions	£35.50m	19.6%
'A' rated institutions	£62.00m	34.1%
Total	**£181.50m**	**100%**
Period – less than one week	£84.00m	46.3%
Period – between one week and one month	£5.00m	2.7%
Period – between one month and three months	£7.00m	3.9%
Period – between three months and 1 year	£85.50m	47.1%
Total	**£181.50m**	**100%**

Risk

3.10 As part of the investment strategy for 2019/20 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 0.014% and 0.023% between April 2019 and September 2019. 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.

3.11 In July 2019, Internal Audit undertook an audit of the treasury management function. The audit concluded that “reasonable assurance” is provided on the effectiveness of the control framework operating and mitigating risks for treasury management. One medium and two low recommendations were provided; one recommendation has already been actioned, and the other two in the process of being actioned.

Compliance with the Annual Investment Strategy

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

Borrowing Strategy

3.13 The council operates separate debt portfolios for the General Fund and the HRA following in introduction of HRA Self Financing in 2012.

3.14 The General Fund has been carrying an internal borrowing position (i.e. where the General Fund borrows cash from its own reserves) since 2008 as a response to the financial crisis. In response to a combination of expectation of increasing interest rate forecasts, the reduction of certain reserves and historically low PWLB borrowing rates, the General Fund has entered into planned borrowing of £27.5m from the PWLB to reduce the internal borrowing position over the last three years. The most recent of this borrowing was undertaken in August 2019, where a £7.5m loan was undertaken for a period of 50 years at a historical low rate of 1.67%. Additionally, £10m of PWLB borrowing was undertaken by the General Fund in March 2019 as part of a debt restructure to replace RBS loans.

3.15 The Housing Revenue Account (HRA) carries a fully funded borrowing position (i.e. the HRA does not borrow from its own reserves, but instead undertakes borrowing for its entire borrowing requirement). Over the last three years, the HRA has entered into a total of £16.5m of external borrowing and £4.5m of borrowing from the General Fund to support the HRA Capital Programme. The most recent of this borrowing was undertaken in August 2019, where a £2.5m loan was undertaken for a period of 50 years at a historical low rate of 1.67%. Additionally, £16m of PWLB borrowing was undertaken by the HRA in March 2019 as part of a debt restructure to replace RBS loans.

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.

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 could enable 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. 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 On 9 October 2019, the government announced an unexpected increase the Public Works Loan Board (PWLB) interest rate for all new loans after 9:30am on the same date. The increase added 1% (100bps) to the cost of borrowing. Loans to local authorities through the PWLB are based on a margin above the gilt rates; during 2019 gilt rates have been at historically low levels meaning the cost of borrowing for councils has been very low. As a result councils have been locking into these cheap rates and the government has seen a significant increase in borrowing leading to the concern the total national PWLB debt would breach its self-imposed government limit. In response to this concern the government has :-

- Increased the overall limit of PWLB debt from £85bn to £95bn;
- Increased the cost of borrowing by 1%.

3.19 The interest rates through the PWLB during 2019 have been much lower than the prudent assumptions used in evaluating council business cases for capital investment in projects such as the housing joint venture or Madeira Terraces and therefore do not put these projects at risk although the step increase does mean there is less contingency/flexibility.

3.20 As a result of the government's announcement to increase rates, other market lenders are now more competitive and will potentially offer better rates than the PWLB, although it is expected market lenders are likely to price using PWLB rates as a reference. Therefore the cost of borrowing for the council will be more expensive than before the rate change from the PWLB. The council has already been contacted by market lenders with competitive lending offers. Officers will explore these other sources of borrowing; although the council has no immediate need to borrow externally.

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

Treasury Advisors

3.22 In November 2018, the council awarded a 13 month contract for treasury advisory services to Link Asset Services (LAS) via an approved framework. This has assisted us in aligning the contract end date with our Orbis partners. Council Officers are currently undertaking a joint procurement exercise with ESCC for a three year contract.

3.23 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 2019. 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 3.7.

Finance Officer Consulted: James Hengeveld Date: 21/11/19

Legal Implications:

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

7.3 The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003/3146 require local authorities to have regard to the CIPFA Code of Practice referred to in paragraph1.3 above when carrying our their functions under Part 1 of the 2003 Act.

7.4 The council’s policy and the actions outlined in the report are considered to comply with the council’s obligations under the Act and wit the afore-mentioned Code.

Lawyer Consulted: Elizabeth Culbert Date: 25/11/19

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 2019 to September 2019
2. The Economy & Interest Rates – Link Asset Services
3. September 2019 Treasury Management statistics

Documents in Members' Rooms

None

Background Documents

1. Part I of the Local Government Act 2003 and associated regulations.
2. The Treasury Management Strategy Statement, Treasury Management Practices and associated schedules 2019/20 (including the Annual Investment Strategy 2019/20) approved by Policy , Resources & Growth Committee on 14 February 2019 and full Council on 28 February 2019.
3. Treasury Management Strategy Statement 2018/19 (including Annual Investment Strategy 2018/19) – Mid-Year Review approved by Policy, Resources & Growth Committee on 6 December 2018.
4. Papers held within Finance, Finance & Resources Directorate.
5. The Prudential Code for Capital Finance in Local Authorities published by CIPFA 2011.