

## **2018/9 Treasury Management Activity Report**

*Director* Netta Meadow, Director – Strategy and Support Services  
*Lead Officer:* Paul Fitzgerald, S151 Officer  
Paul Matravers, Specialist - Finance  
*Contact Details:* Paul.fitzgerald@southsomerset.gov.uk or (01935) 462226  
Paul.matravers@southsomerset.gov.uk or (01935) 462275

### **Purpose of Report**

1. To review the treasury management activity and the performance against the Prudential Indicators for the 2018/19 financial year as prescribed by the CIPFA Code of Practice and in accordance with the Council's Treasury Strategy, Annual Investment Policy and Treasury Management Practices.

### **Recommendations**

2. The Audit Committee is recommended to:
  - Note the Treasury Management Activity for the 2018/19 financial year;
  - Note the position of the individual prudential indicators for the 2018/19 financial year;
  - Note the outlook for the investment performance in 2018/19;
  - Note the council operated within all of the Prudential Indicators during 2018/19;
  - Recommend the 2018/19 Treasury Management Activity Report to full Council

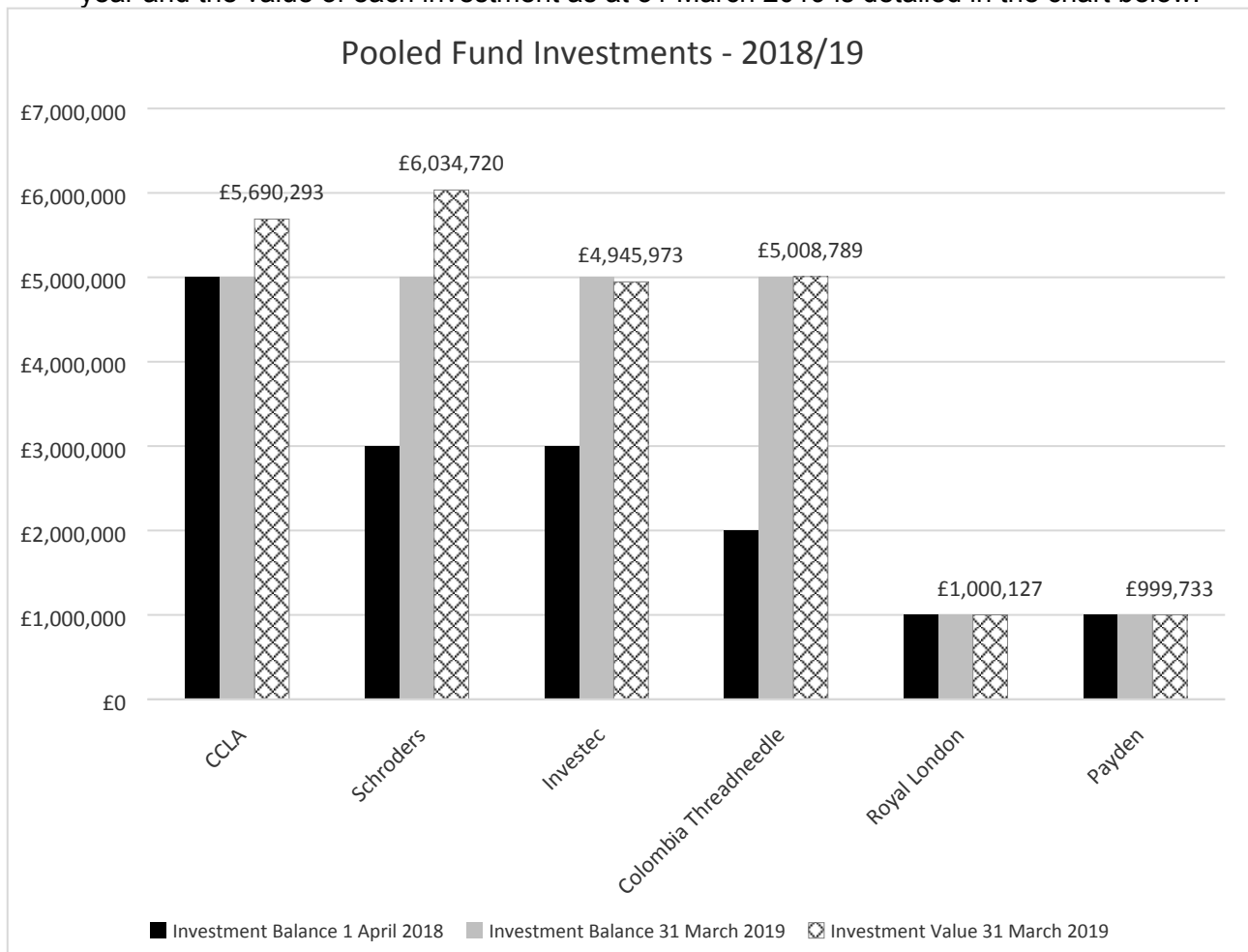
### **Background**

3. Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year and, as a minimum, produce a six month and annual treasury outturn report. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code. The Council reports six monthly to Full Council against the strategy approved for the year. The scrutiny of treasury management policy, strategy and activity is delegated to the Audit Committee.
4. The Council's Treasury Management Strategy for 2018/19 was approved by Full Council on 22 February 2018. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Council's Treasury Management Strategy.
5. The 2017 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 26 February 2019.
6. Overall responsibility for treasury management remains with the Council. The day to day treasury management operation is delegated to the S151 Officer and is undertaken by the Finance function which is part of the Strategy and Support Services directorate. No treasury management activity is without risk; the effective identification and management of risk are integral to the Council's treasury management objectives.

7. This report provides information on the performance of the Council's Treasury Investments in 2018/19. The performance of the Council's Commercial Investments which are part of the Commercial strategy are not included in this report.

### Investment Activity

8. The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2018/19, the Council's investment balance ranged between £30 million and £50 million.
9. Both the CIPFA Code and government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.
10. The Council's best performing investments in 2018/19 were the investments in the Pooled Funds (Strategic Investments). details of the investment balance at the start and end of the financial year and the value of each investment as at 31 March 2019 is detailed in the chart below.



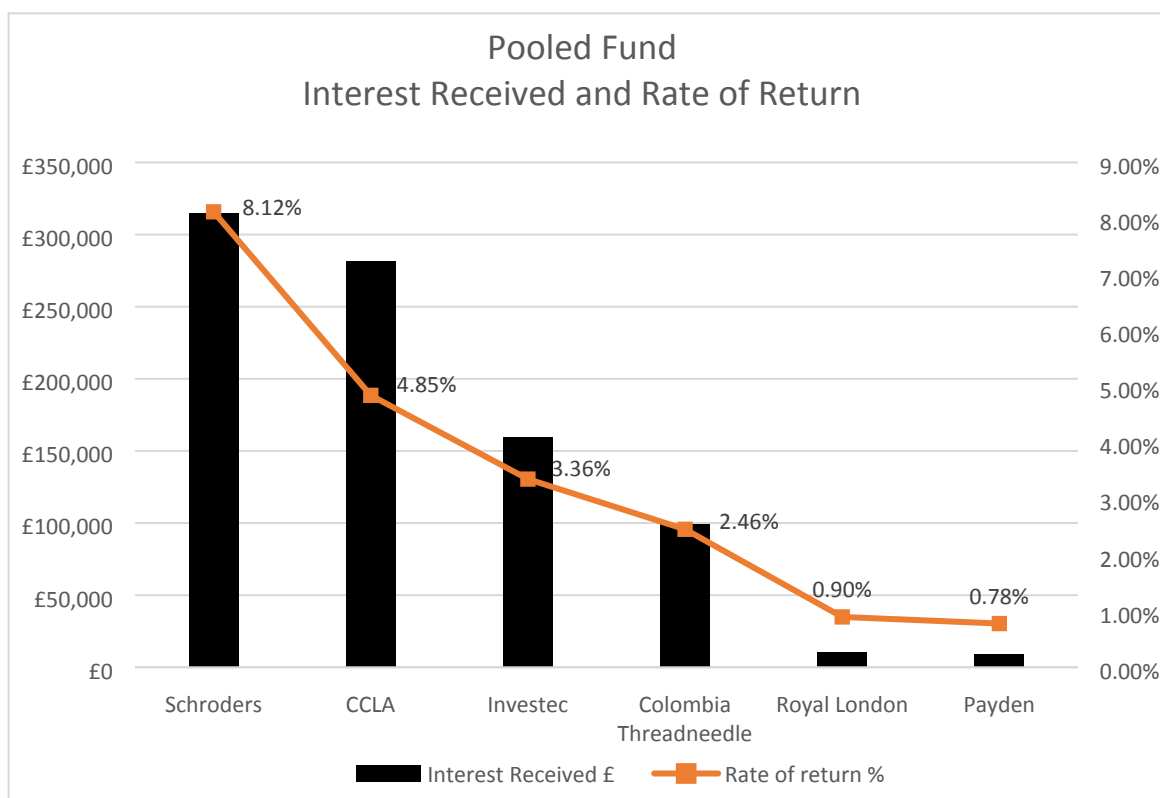
**Note:** Pooled fund investments are revalued at the end of the financial year to reflect the fair value of the investment, the third bar in the graph signifies this value and details the investment value as at 31 March 2019. The first and second bars represent the investment balance in each fund at that date.

### Pooled Fund Investments 2018/19

The table below includes the opening and closing investment balances for each pooled fund investment. The investment fair value signifies the individual value of the investments after the year end revaluation.

Investment Type	Investment Balance			Investment Fair Value	
	01-Apr-18	31-Mar-19		01-Apr-18	31-Mar-19
CCLA	£5,000,000	£5,000,000		£5,603,228	£5,690,293
Schrodgers	£3,000,000	£5,000,000		£2,984,650	£6,034,720
Investec	£3,000,000	£5,000,000		£2,948,061	£4,945,973
Colombia Threadneedle	£2,000,000	£5,000,000		£2,000,000	£5,008,789
Royal London	£1,000,000	£1,000,000		£999,119	£1,000,127
Payden	£1,000,000	£1,000,000		£1,000,713	£999,733
<b>Total</b>	<b>£15,000,000</b>	<b>£22,000,000</b>		<b>£15,535,771</b>	<b>£23,679,635</b>

The income generated from these investments in 2018/19 and the rate of return is detailed in graph and table below.



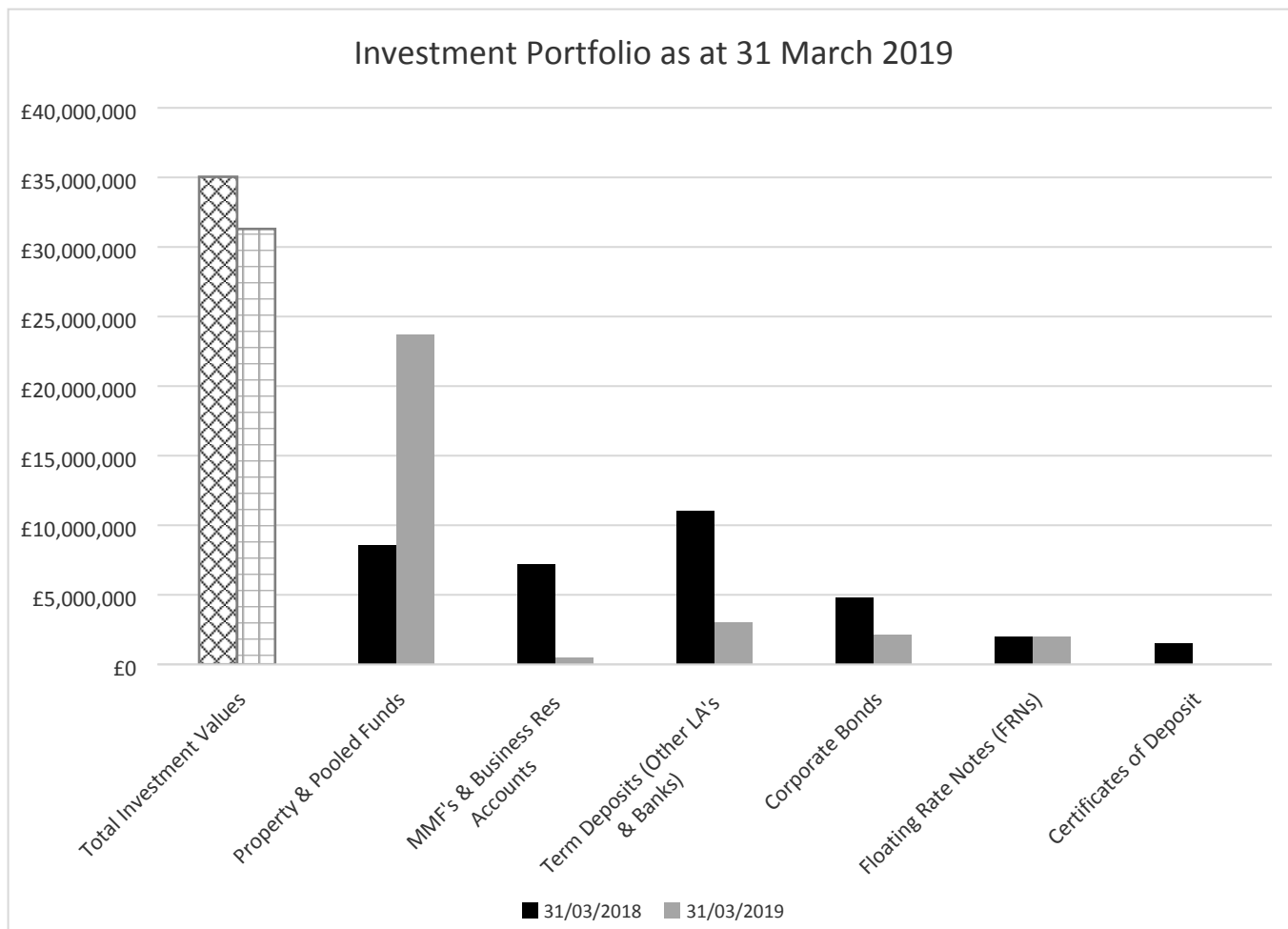
Fund	Interest Received £	Rate of return %
Schrodgers	315,013	8.12%
CCLA	281,579	4.85%
Investec	159,202	3.36%
Colombia Threadneedle	99,147	2.46%
Royal London	10,427	0.90%
Payden	9,058	0.78%
<b>Total</b>	<b>874,425</b>	<b>4.21%</b>

11. Pooled funds have no defined maturity date, but are available for withdrawal after a notice period. Their performance and continued suitability in meeting the Council's investment objectives is



## Investment Portfolio – Values and Returns

17. The graph below provides a snapshot of the Council's portfolio of investments at the end of the 2018/19 financial year, in comparison to the previous year end position.



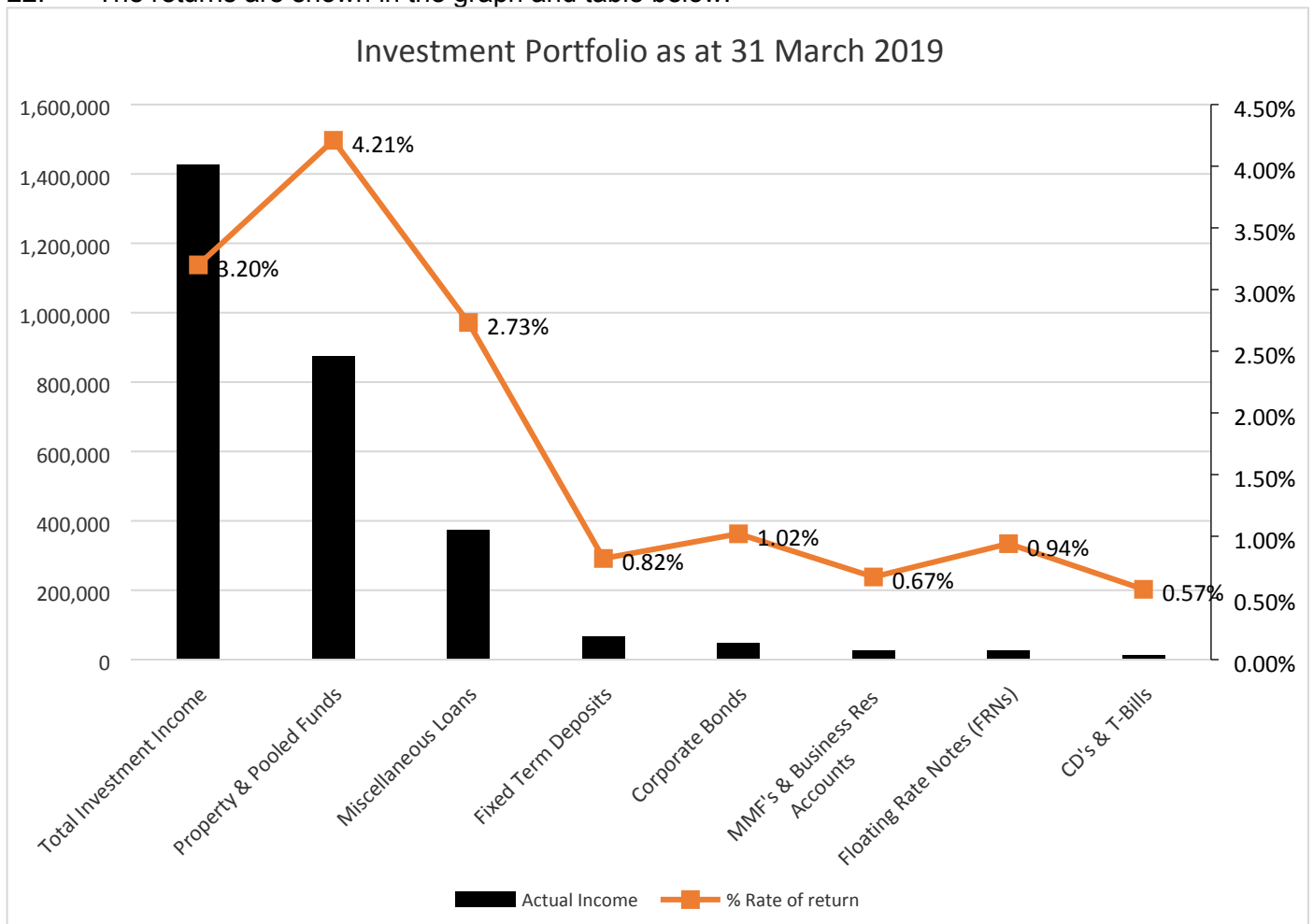
18. The table below provides additional information on the actual value of investments at the start and end of the 2018/19 financial year:

Investment type	Investment Value as at 31/03/2018 £	Investment Value as at 31/03/2019 £	Actual Income £	Rate of return %
Property & Pooled Funds	8,551,289	23,679,635	874,425	4.21%
Money Market Funds & Business Reserve Accounts	7,214,482	479,810	25,772	0.67%
Term Deposits (Other LA's & Banks)	11,000,000	3,000,000	67,138	0.82%
Corporate Bonds	4,767,078	2,129,992	46,684	1.02%
Floating Rate Notes (FRNs)	2,008,716	2,006,968	25,100	0.94%
Certificates of Deposit	1,502,877	0	12,458	0.57%
<b>Total Investment Values</b>	<b>35,044,442</b>	<b>31,296,405</b>	<b>1,039,119</b>	<b>3.20%</b>

19. The Council's year end investments as at 31 March 2019 were £3.75m less than as at 31 March 2018, Investments arise due to timing differences in expenditure being made and income being received, this can mean that the year end investment balance can be slightly less or more than the previous financial year. The reduction in investments is not due to a change in the Council's investment policy.
20. There is a significant difference in the types of investment that the Council held at the 31 March 2018 and 31 March 2019. As mentioned above, the switch to higher yielding, long term strategic investments have resulted in a large portion of the Council's investment being concentrated in the pooled and property fund investment type. Pooled and property fund investments amounted to 76% of the investment portfolio as at 31 March 2019 (24% as at 31 March 2018).
21. The Council has worked closely with Arlingclose on the investment diversification, Arlingclose are comfortable with the percentage of investment that the Council holds in pooled and property funds. The Council continually monitors the performance of the property and pooled funds and is able to withdraw funds at short notice if the fund performance were to deteriorate. Equally, the Council may borrow short term to manage cash flow variations if necessary.

### Returns achieved in 2018/19

22. The returns are shown in the graph and table below:



<b>Investment type</b>	<b>Actual Income £</b>	<b>Rate of return %</b>
Property & Pooled Funds	874,425	4.21%
Miscellaneous Loans	373,279	2.73%
Fixed Term Deposits	67,138	0.82%
Corporate Bonds	46,684	1.02%
Money Market Funds & Business Reserve Accounts	25,772	0.67%
Floating Rate Notes (FRNs)	25,100	0.94%
Certificates of Deposit & T-Bills	12,458	0.57%
<b>2018/19 Treasury Investment Income</b>	<b>1,424,856</b>	<b>3.20%</b>
<b>2018/19 Treasury Income Budget</b>	<b>763,530</b>	
<b>Surplus</b>	<b>661,326</b>	

23. The table above shows investment income for the year compared to the budget. The figures show a significant surplus over budget of £661,326. The original treasury management budget of £763,530 was derived by forecasting an average rate of return of 1.52% based on an average investment portfolio of £48m. The actual average investment return achieved during the year was 3.20%, and the average portfolio balance was £40m.
24. The surplus over budget is as a result of a number of factors, the main factors being:
- Additional interest received due to the diversification into long term strategic investments
  - A new loan for service purposes has been made in year resulting in additional interest.
25. The outturn position is also affected by both the amount of cash we have available to invest and the interest base rate set by the Bank of England. Balances are affected by the timing of revenue and capital income and expenditure, and the collection and distribution of council tax and business rates income.

### Treasury Investments

26. Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2018/19. The table below lists the investments held on 31 March 2019.

### Breakdown of investments as at 31 March 2019

<b>Date Invested</b>	<b>Counterparty</b>	<b>Nominal Amount</b>	<b>Rate %</b>	<b>Maturity Date</b>
11 Nov 16	Northumberland County Council	1,000,000	1.00	11 Nov 20
09 Feb 17	Liverpool City Council	2,000,000	0.92	11 Nov 19
	<b>Corporate Bonds</b>			
20 Oct 16	Santander UK Plc *Covered*	1,000,000	1.04	14 Apr 21
10 Nov 16	National Australia Bank *Covered*	1,000,000	1.10	10 Nov 21
	<b>Floating Rate Notes (FRN's)</b>			
16 Jan 17	Lloyds Bank Plc *Covered*	1,600,000	0.99	16 Jan 20
16 Jan 17	Lloyds Bank Plc *Covered*	400,000	0.98	16 Jan 20
	<b>Money Market Funds</b>			
	Aberdeen (previously Standard Life)	480,000	0.53	
	<b>Property &amp; Pooled Funds</b>			
	Payden Fund VNAV	1,000,000	0.78	

Date Invested	Counterparty	Nominal Amount	Rate %	Maturity Date
	Royal London Cash Plus Fund	1,000,000	0.58	
	CCLA Property Fund	5,000,000	3.62	
	Investec Diversified Income Fund	5,000,000	2.99	
	Schroder Income Maximiser Fund	6,250,000	5.69	
	Colombia Threadneedle Equity Income Fund	5,000,000	2.15	
	<b>TOTAL</b>	<b>30,730,000</b>		

Note: Money Market Funds are instant access accounts so the rate displayed is a daily rate

## Non-Treasury Investments

27. The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return.

The Council also held £11.24m of such investments in

- Loan to Community Organisation - £0.17m
- Loan to Local Authority Partnership - £1.23m
- Loan for Commercial Activities - £9.84m

## Borrowing

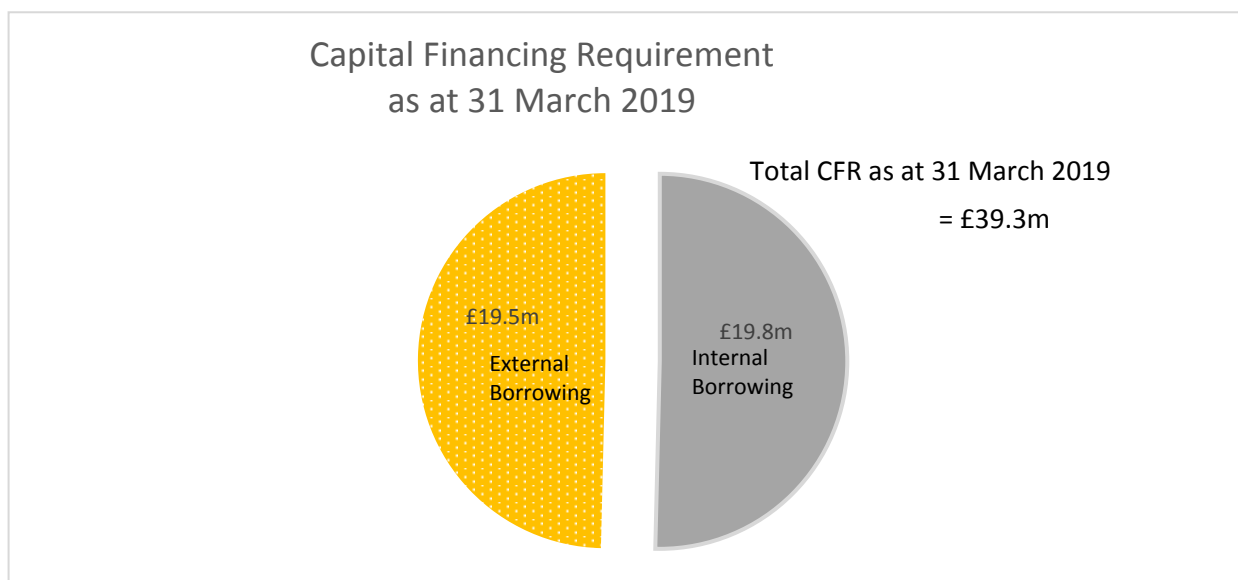
28. The Council's primary objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective.
29. In keeping with these objectives, new borrowing was kept to a minimum, with the longest duration being a 69 day period. This strategy enabled the Council to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.
30. As at 31 March 2019 the Council had external borrowing of £19,500,000 as part of its strategy for funding the capital programme and the purchase of commercial property.
31. Details of the borrowing are included in the table below.

Lender	Date Borrowed	Maturity Date	No of Days	Interest Rate	Amount £	2018/19 Interest £	Total Interest £
The Vale of Glamorgan Council	22/01/19	01/04/19	69	0.79%	1,500,000	2,240	2,240
Derbyshire County Council Pension Fund	15/02/19	01/04/19	45	0.90%	10,000,000	11,096	11,096
Coventry University	18/03/19	18/04/19	31	0.90%	8,000,000	2,762	6,115
				<b>Total</b>	<b>19,500,000</b>	<b>16,098</b>	<b>19,451</b>



32. With short-term interest rates remaining much lower than long-term rates, the Council considered it to be more cost effective in the near term to use internal resources in parallel with short-term loans.
33. The Council's underlying need to borrow is defined as its 'Capital Financing Requirement (CFR)'. The CFR was £17.4 million at the beginning of 2018/19. Capital expenditure during 2018/19 was funded through a combination of capital receipts, revenue reserves, external contributions (e.g. S106 receipts) and borrowing. As a result, the borrowing requirement (CFR) has increased to £39.3 million. However, we have followed a strategy of using our cash reserves to finance this borrowing requirement in the short term – known as “internal borrowing” – as short term investment returns foregone are currently lower than longer term borrowing rates.

	£millions	%
Internal Borrowing	£19.8m	50.4%
External Borrowing	£19.5m	49.6%
<b>Capital Financing Requirement as at 31 March 2019</b>	<b>£39.3m</b>	



### Prudential Indicators – 2018/19

34. In February 2018, through approval of the Treasury Management Strategy Full Council approved the Prudential Indicators for 2018/19, as required by the Prudential Code for Capital Finance in Local Authorities. The Local Government Act 2003 allows local authorities to determine their own borrowing limits provided they are affordable and that every local Council complies with the Code.

### Prudential Indicator 1 - Capital Expenditure:

35. The actual capital expenditure incurred for 2018/19 compared to the revised estimate was:

	2017/18 Outturn £'000	2018/19 Revised Estimate £'000	2018/19 Outturn £'000	2018/19 Variance £'000	Reason for Variance
Approved capital schemes	16,424	33,652	28,414	(5,237)	Timing of investment property acquisitions
<b>Total Expenditure</b>	<b>16,424</b>	<b>33,652</b>	<b>28,414</b>	<b>(5,237)</b>	

### Prudential Indicator 2 - Ratio of Financing Costs to Net Revenue Stream:

36. A comparison needs to be made between financing capital costs and the revenue income stream to support these costs. This shows how much of the revenue budget is committed to the servicing of finance.

	2017/18 Outturn £'000	2018/19 Revised Estimate £'000	2018/19 Outturn £'000	2018/19 Variance £'000	Reason for Variance
Financing Costs	(434)	(613)	(1,047)	(434)	Additional investment income from the Pooled Funds
Net Revenue Stream	17,798	16,608	16,348	(260)	
%	<b>(2.4%)</b>	<b>(3.7%)</b>	<b>(6.4%)</b>	<b>(2.7%)</b>	

\*figures in brackets denote income through receipts and reserves

37. The financing costs include interest payable and notional amounts set aside to repay debt less interest on investment income. The figure in brackets is due to investment income outweighing financing costs significantly for the Council but is nevertheless relevant since it shows the extent to which the Council is dependent on investment income.

### Prudential Indicator 3 - Capital Financing Requirement:

38. The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. The year-end capital financing requirement for the council is shown below:

	2017/18 Outturn £'000	2018/19 Original Estimate £'000	2018/19 Outturn £'000	2018/19 Variance £'000	Reason for Variance
Opening CFR	9,338	25,499	17,439	(8,060)	
Capital Expenditure	16,926	31,204	28,414	(2,790)	Capital schemes part funded through internal borrowing in 2018/19
Capital Receipts*	(6,337)	(8,325)	(4,560)	3,765	
Grants/Contributions*	(2,319)	(2,879)	(1,711)	1,168	

Minimum Revenue Position (MRP)	(169)	(260)	(221)	39	MRP towards borrowing for commercial investments
Additional Leases taken on during the year	0	0	0	0	
<b>Closing CFR</b>	<b>17,439</b>	<b>45,239</b>	<b>39,361</b>	<b>(5,878)</b>	

\*Figures in brackets denote income through receipts or use of revenue resources.

**Prudential Indicator 4 – Gross Debt and the Capital Financing Requirement:**

39. The Council is also required to ensure that any medium term borrowing is only used to finance capital and therefore it has to demonstrate that the net external borrowing does not, except in the short term, exceed the total of capital financing requirements over a three year period.

	<b>2017/18 Outturn £'000</b>	<b>2018/19 Revised Estimate £'000</b>	<b>2018/19 Outturn £'000</b>	<b>2018/19 Variance £'000</b>
Borrowing	0	30,000	19,500	(10,500)
Finance Leases	138	100	82	(18)
<b>Total Debt</b>	<b>138</b>	<b>30,100</b>	<b>19,582</b>	<b>(10,518)</b>
Capital Financing Requirement	17,439	45,239	39,361	(5,878)

40. Total debt is expected to remain below the CFR for the foreseeable future.

**Prudential Indicator 5 - Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure:**

41. The Council must set three years of upper limits to its exposure to the effects of changes in interest rates. As a safeguard, it must ensure that its limit would allow it to have up to 100% invested in variable rate investments to cover against market fluctuations. For this purpose, term deposits of less than 365 days are deemed to be variable rate deposits. Fixed rate deposits are investments in Eurobonds, Corporate Bonds and term deposits exceeding 365 days.

<b>Investment</b>	<b>2017/18 Actual %</b>	<b>2018/19 % Limit</b>	<b>2018/19 Actual %</b>
Fixed	20.45	100%	57.14
Variable	79.55	100%	42.86

42. The Council must also set limits to reflect any borrowing we may undertake.

<b>Borrowing</b>	<b>2017/18 Actual %</b>	<b>2018/19 % Limit</b>	<b>2018/19 Actual %</b>
Fixed	0	100%	100%
Variable	0	100%	0

43. The indicator above has been set at 100% to maximise opportunities for future debt as they arise.

**Prudential Indicator 6 - Upper Limit for total principal sums invested over 364 days:**

44. The Council must also set upper limits for any investments of longer than 364 days. The purpose of this indicator is to ensure that the Council, at any time, has sufficient liquidity to meet all of its financial commitments.

<b>Upper Limit for total principal sums invested over 364 days</b>	<b>2017/18 Actual (Principal amount) £'000</b>	<b>2018/19 Maximum Limit £'000</b>	<b>2018/19 Actual (Principal amount) £'000</b>
Between 1-2 years	4,000	50,000	6,000
Between 2-3 years	1,000		1,000
Between 3-4 years	2,000		0
Between 4-5 years	0		0
Over 5 years	0		0
<b>Total</b>	<b>7,000</b>	<b>50,000</b>	<b>7,000</b>

45. The table above shows that the Council adopts a policy of safeguarding its investments by minimising investments that are redeemable more than five years ahead.

**Prudential Indicator 7 – Credit Risk:**

46. The Council considers security, liquidity and yield, in that order, when making investment decisions.
47. Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the Council’s assessment of counterparty credit risk. The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:
- Published credit ratings of the financial institution and its sovereign
  - Sovereign support mechanisms
  - Credit default swaps (where quoted)
  - Share prices (where available)
  - Economic Fundamentals, such as a country’s net debt as a percentage of its GDP
  - Corporate developments, news articles, markets sentiment and momentum
  - Subjective overlay
48. The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

### Prudential Indicator 8 - Actual External Debt:

49. This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities (this represents our finance leases). This indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

<b>Actual External Debt as at 31/03/2019</b>	<b>£'000</b>
Borrowing	19,500
Other Long-term Liabilities (Finance Leases)	
- Vehicles	82
- Photocopiers	0
<b>Total</b>	<b>19,582</b>

### Prudential Indicator 9 - Authorised Limit for External Debt:

50. This limit represents the maximum amount that the Council may borrow at any point in time during the year. If this limit is exceeded the Council will have acted ultra vires. It also gives the Council the responsibility for limiting spend over and above the agreed capital programme. A borrowing requirement was identified in year to finance the capital programme and further borrowing may be undertaken to fund the agreed plans to acquire investment properties. [Note the borrowing limit has increased during 2018/19]

	<b>2017/18 Actual £'000</b>	<b>2018/19 Original Estimate £'000</b>	<b>2018/19 Actual £'000</b>
Borrowing	0	124,000	19,500
Other Long-term Liabilities	138	1,000	82
<b>Total</b>	<b>138</b>	<b>125,000</b>	<b>19,582</b>

### Prudential Indicator 10 – Operational Boundary for External Debt:

51. The operational boundary sets the limit for short term borrowing requirements for cash flow and has to be lower than the previous indicator, the authorised limit for external debt.
52. Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

53. The S151 Officer has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next Council meeting.

	<b>2017/18 Actual £'000</b>	<b>2018/19 Original Estimate £'000</b>	<b>2018/19 Actual £'000</b>	<b>2018/19 Variance £'000</b>
Borrowing	0	30,000	19,500	(10,500)
Other Long-term Liabilities	138	800	82	(718)
<b>Total</b>	<b>138</b>	<b>30,800</b>	<b>19,582</b>	<b>(11,218)</b>

#### **Prudential Indicator 11 - Maturity Structure of Fixed Rate borrowing:**

54. This indicator is relevant when we borrow, then we can take a portfolio approach to borrowing in order to reduce interest rate risk. This indicator is shown as the Council has set limits in anticipation of future borrowing.

<b>Maturity structure of fixed rate borrowing</b>	<b>2018/19 Upper Limit %</b>	<b>2018/19 Lower Limit %</b>	<b>2018/19 Actual %</b>
Under 12 months	100	100	100
12 months and within 24 months	100	100	0
24 months and within 5 years	100	100	0
5 years and within 10 years	100	100	0
10 years and above	100	100	0

#### **Compliance**

55. The council operated within all of the Prudential Indicators during 2018/19.

#### **Background Papers:**

Treasury Management Strategy Statement 2018/19  
Prudential Indicators and MRP Statement 2018/19  
Capital Outturn 2018/19

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