

NORTH DEVON COUNCIL

REPORT TO: STRATEGY AND RESOURCES

Date: 4th NOVEMBER 2019

TOPIC: Treasury Management Strategy Statement and Annual Investment Strategy

MID-YEAR REVIEW REPORT 2019/20

REPORT BY: CHIEF FINANCIAL OFFICER

1. INTRODUCTION

1.1 This mid year report has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the first part of the 2019/20 financial year (appendix A);
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure and prudential indicators;
- A review of the Council's investment portfolio for 2019/20;
- A review of the Council's borrowing strategy for 2019/20;
- A review of any debt rescheduling undertaken during 2019/20;
- A review of compliance with Treasury and Prudential Limits for 2019/20.

2. RECOMMENDATIONS

The Committee is asked to recommend to full Council that:

- 2.1 The changes to the prudential indicators be approved.
- 2.2 The report and the treasury activity be noted.

3. REASONS FOR RECOMMENDATIONS

3.1 This Council is required through regulations issued under the Local Government Act 2003 to produce a mid year treasury report reviewing treasury management activities and the prudential and treasury indicators for 2019/20. This report meets the requirements of the CIPFA Code of Practice on Treasury Management (revised 2017).

3.2 This Council is also required under the Code to give prior scrutiny to the treasury management reports by the Policy Development Committee before they are reported to the full Council.

4. REPORT

4.1 Treasury Management Strategy Statement and Annual Investment Strategy update

The Treasury Management Strategy Statement (TMSS) for 2019/20 was approved by this Council on 25th February 2019.

The underlying TMSS approved previously requires revision in the light of economic and operational movements during the year. The proposed changes are set out below:

| Prudential Indicator 2019/20 | Original Estimate £000 | Revised Prudential Indicator £000 |
|--|-----------------------------------|--|
| Capital Financing Requirement | 6,440 | 5,462 |
| Authorised Borrowing Limit | 11,000 | 22,500 |
| Maturity Structure of Debt over 10 years | 50% | 90% |

Section 4.3 of this report gives further information on the Capital Financial Requirement. The Authorised borrowing limit and the maturity structure of debt over 10 years have been amended to reflect the Leisure Centre capital project.

4.2 The Council's Capital Position (Prudential Indicators)

This part of the report is structured to update:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

Prudential Indicator for Capital Expenditure

This table shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the budget.

| Capital Expenditure by Service | 2019/20 Original Estimate £000 | Current Position 30/09/19 £000 | 2019/20 Revised Estimate £000 |
|---------------------------------------|---|---|--|
| Chief Executive & Corporate | 675 | 41 | 748 |
| Corporate & Community | 3,095 | 1,186 | 3,741 |
| Environmental Health & Housing | 2,602 | 415 | 2,004 |
| Operational Services | 1,209 | 190 | 449 |
| Place | 1,044 | 112 | 1,189 |
| Resources | 984 | 464 | 880 |
| Total | 9,609 | 2,408 | 9,011 |

Changes to the Financing of the Capital Programme

The table below draws together the main strategy elements of the capital expenditure plans (above), highlighting the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure. The borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

| Capital Expenditure | 2019/20 Original Estimate £000 | 2019/20 Revised Estimate £000 |
|------------------------------|---|--|
| Supported | 0 | 0 |
| Unsupported | 9,609 | 9,011 |
| Total spend | 9,609 | 9,011 |
| Financed by: | | |
| Capital receipts | (650) | (650) |
| Capital grants | (6,074) | (6,230) |
| Capital reserves | (1,316) | (871) |
| Total financing | (8,040) | (7,751) |
| Borrowing requirement | 1,569 | 1,260 |

4.3 Changes to the Prudential Indicators for the Capital Financing Requirement, External Debt and the Operational Boundary

The table below shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period, which is termed the Operational Boundary.

Prudential Indicator – Capital Financing Requirement

The forecast Capital Financing Requirement has reduced as a result of slippages to the capital programme as shown below. For example the projects for the Pannier Market Roof and Recycling Process Hall Infrastructure have now moved into 2020/21.

Prudential Indicator – the Operational Boundary for external debt

| | 2019/20 Original Estimate £000 | 2019/20 Revised Estimate £000 |
|--|---|--|
| Prudential Indicator – Capital Financing Requirement | | |
| Total CFR | 6,440 | 5,462 |
| Movement in CFR from 1/4/19 | | 751 |
| Prudential Indicator – the Operational Boundary for external debt | | |
| Borrowing | 2,500 | 1,250 |
| Other long term liabilities | 0 | 0 |
| Total debt (year-end position) | 2,500 | 1,250 |

4.4 Limits to Borrowing Activity

The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2019/20 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need, which will be adhered to if this proves prudent.

| | 2019/20 Original Estimate £000 | Current Position 30/09/19 £000 | 2019/20 Revised Estimate £000 |
|-----------------------------------|---|---|--|
| Gross borrowing | 2,500 | 1,250 | 1,250 |
| Plus: other long term liabilities | 0 | 0 | 0 |
| Total debt | 2,500 | 1,250 | 1,250 |
| CFR (year end position) | 6,440 | | 5,462 |

The Chief Financial Officer reports that no difficulties are envisaged for the current or future years in complying with this prudential indicator.

A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit that represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

| Authorised limit for external debt | 2019/20 Original Indicator £000 | 2019/20 Revised Indicator £000 |
|---|--|---|
| Borrowing | 10,500 | 22,000 |
| Other long term liabilities | 500 | 500 |
| Total | 11,000 | 22,500 |

The Leisure Provision at Seven Brethren report considered by Full Council on 13th March 2019, approved the increase in authorised borrowing limit to £22m from 2020/21. Amending the authorised borrowing limit now will provide some flexibility for limited early borrowing for the Leisure Centre capital project, if prudent to do so.

4.5 Investment Portfolio 2019/20

Treasury Management Investments

In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. As set out in appendix A, it is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the current 0.75% Bank Rate. The continuing potential for a re-emergence of a Eurozone sovereign debt crisis, and its impacts on banks, prompts a low risk and short term strategy. Given this risk

environment and the fact that increases in Bank Rate are likely to be gradual and unlikely to return to the levels seen in previous decades, investment returns are likely to remain low.

The Council held £18.6m of investments as at 30 September 2019 (£8.56m at 31 March 2019) and the investment portfolio yield for the first six months of the year was 0.70% against the benchmark 7 day LIBID of 0.57%.

The Chief Financial Officer confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2019/20.

The Council's budgeted investment return for 2019/20 was £70,000. As at 30th September 2019 £62,203 investment interest was earned in the half-year period.

Investment Counterparty Criteria

The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function.

Non-Treasury Management Investments

The major changes required by the 2017 Treasury Management and Prudential Codes relate to non-treasury investments in other financial assets and property, primarily for financial return.

The Council is currently considering a more detailed commercialisation strategy and a report will be coming to Members in due course.

Whilst the Council currently has no plans for material investments in property or other financial assets during 2019/20, it has purchased a light industrial unit at Seven Brethren and will consider other small scale opportunities if appropriate.

4.6 Borrowing

The Council's capital financing requirement (CFR) for 2019/20 is £5.46m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the Public Works Loan Board (PWLB), or the market (external borrowing), or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions.

At present, the Council has projected total external borrowing of £1.25m and utilising £4.21m of cash flow funds in lieu of borrowing. This is a prudent and cost effective approach in the current economic climate but will require ongoing monitoring of economic conditions.

It is not anticipated that further borrowing will be undertaken during this financial year but that will be dependent on the progress of the Leisure Centre project and movements in PWLB / market borrowing rates during the second half of the financial year.

Total Borrowing:

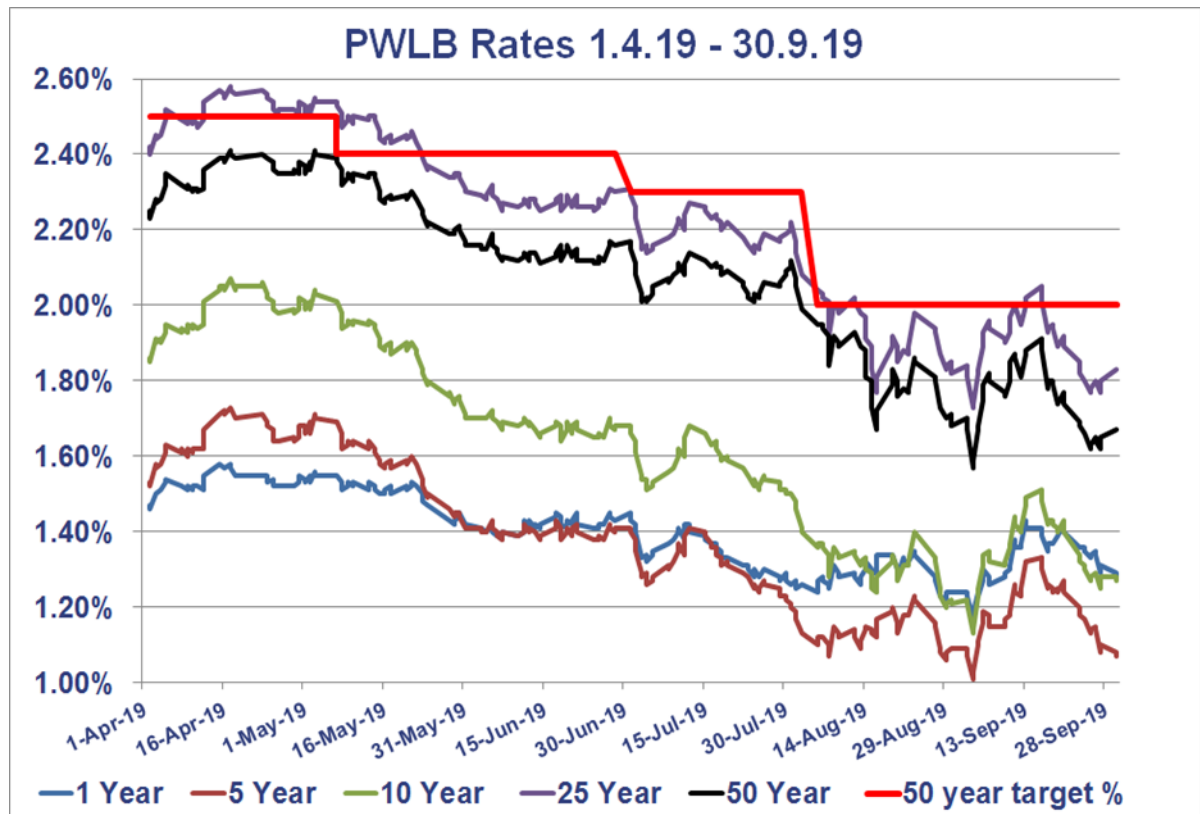
| Lender | Principal (£000) | Type | Interest Rate | Loan period | Maturity date |
|--------|------------------|---------------------|---------------|-------------|---------------|
| PWLB | £750 | Fixed interest rate | 2.44% | 5.6 years | May 2020 |
| PWLB | £500 | Fixed interest rate | 1.43% | 10 years | Aug 2026 |

The graph and table below show the movement in PWLB certainty rates for the first six months of the year to date. PWLB rates have been on a falling trend during this period and longer rates have almost halved to reach historic lows. The 50 year PWLB target (certainty) rate for new long term borrowing fell from 2.50% to 2.00% during this period.

During October 2019, HM Treasury announced, with immediate effect, that it was increasing the margin that applies to new loans from the PWLB by 100bps (one percent) on top of usual lending terms. This is in part due to some local authorities substantially increasing their use of the PWLB in recent months, as the cost of borrowing has fallen to record lows. This has effectively restored interest rates to the levels available in 2018.

We will continue to monitor how the markets react to this change and the implications for any future borrowing.

PWLB certainty rates 1 April 2019 to 30 September 2019



| | 1 Year | 5 Year | 10 Year | 25 Year | 50 Year |
|---------|------------|------------|------------|------------|------------|
| Low | 1.17% | 1.01% | 1.13% | 1.73% | 1.57% |
| Date | 03/09/2019 | 03/09/2019 | 03/09/2019 | 03/09/2019 | 03/09/2019 |
| High | 1.58% | 1.73% | 2.07% | 2.58% | 2.41% |
| Date | 15/04/2019 | 17/04/2019 | 17/04/2019 | 17/04/2019 | 17/04/2019 |
| Average | 1.40% | 1.37% | 1.62% | 2.20% | 2.07% |

4.7 Debt Rescheduling

No debt rescheduling was undertaken during the first six months of 2019/20.

5. RESOURCE IMPLICATIONS

5.1 As detailed in the report.

6. EQUALITIES ASSESSMENT

6.1 There are not any equalities implications anticipated as a result of this report, as the purpose of this report is to present the Council's financial position only.

7. CONSTITUTIONAL CONTEXT

| Article and paragraph | Referred or delegated power? |
|---|------------------------------|
| Part 4 Financial Procedure Rules (Article 13.8) | Delegated |
| Article 4.4 | |

8. STATEMENT OF CONFIDENTIALITY

8.1 This report contains no confidential or exempt information under the provisions of Schedule 12A of 1972 Act.

9. BACKGROUND PAPERS

9.1 Background papers will be available for inspection and will be kept by the author of the report.

10. STATEMENT OF INTERNAL ADVICE

10.1 The author (below) confirms that advice has been taken from all appropriate Councillors and Officers.

Author: Jon Triggs, Head of Resources

Date: 15th October 2019

Reference: T:\Technical\Adam\Treasury Management\ TM Mid Year Report 2019_20.doc