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<b>Report To:</b>	<b>Policy &amp; Resources Committee</b>	<b>Date:</b>	<b>11 August 2020</b>
<b>Report By:</b>	<b>Chief Financial Officer</b>	<b>Report No:</b>	<b>FIN/56/20/AP/LA</b>
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<b>Subject:</b>	<b>TREASURY MANAGEMENT – ANNUAL REPORT 2019/20</b>		

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## **1.0 PURPOSE**

- 1.1 The purpose of this report is to advise the Committee of the operation of the treasury function and its activities for 2019/20 as required under the terms of Treasury Management Practice 6 ("TMP6") on "Reporting Requirements and Management Information Arrangements".

## **2.0 SUMMARY**

- 2.1 As at 31 March 2020 the Council had gross external debt (including PPP) of £274,392,487 and investments of £29,655,497. This compares to gross external debt (including PPP) of £259,305,590 and investments of £18,915,222 at 31 March 2019.
- 2.2 The Council's Capital Financing Requirement at 31 March 2020 was £302,233,000. The gross external debt was £27,840,513 (9.2%) less than the Capital Financing Requirement meaning that the Council was in an underborrowed position (and remains so in 2020/21). This position is attributable to the level of cash-backed reserves held by the Council.
- 2.3 The Loans Fund Pool Rate for 2019/20 was lower than that in 2018/19 and at its lowest level since before Local Government reorganisation.
- 2.4 The average rate of return achieved on investments during 2019/20 was 0.867% which exceeds the benchmark return rate for the year of 0.634% by 0.233% and resulted in £51,300 of additional interest on investments for the Council.
- 2.5 The Council operated within the required treasury limits and Prudential Indicators for the year set out in the Council's Treasury Policy Statement, annual Treasury Strategy Statement, and the Treasury Management Practices.
- 2.6 The Covid-19 crisis has added to economic uncertainty in the UK and around the world, resulting in continuing volatility in the financial markets and uncertainty on UK interest rates. The economic situation continues to be closely monitored.

## **3.0 RECOMMENDATIONS**

- 3.1 It is recommended that the Committee notes the contents of the annual report on Treasury Management for 2019/20 and the ongoing work to seek to ensure the delivery of financial benefits for the Council during the current uncertainty and beyond.
- 3.2 It is recommended that the Committee notes that the report will be remitted to the Full Council for approval.

Alan Puckrin  
Chief Financial Officer

## **4.0 BACKGROUND**

- 4.1 The Council is required by regulations issued under the Local Government in Scotland Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2019/20.
- 4.2 Treasury Management in this context is defined as: "The management of the local authority's cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."
- 4.3 This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code). The report also includes a section on Loan Fund Advances (section 7) which includes information required by regulations that came into effect on 1 April 2016.

## **5.0 ANNUAL REVIEW**

- 5.1 The treasury management issues arising during the year were:
  - a. The Council's debt (including PPP) increased during the year by £15.086m whilst Council investments increased by £10.740m. The Council borrowed £32m during the year. Of this, £20m was to cover maturing debt that was repaid this year and in previous years whilst £12m was new borrowing including £2m in April 2019 at a reduced rate available for the Gourrock Primary School extension and £10m of 1 year borrowing in March 2020 for additional liquidity to cover payments expected to arise due to Covid-19.
  - b. The Council remained within its Prudential Indicator and Treasury Management limits during 2019/20.
  - c. As at 31 March 2020 the Council had under borrowed against its capital financing requirement by £27.841m. This under borrowing is lower than in 2018/19 due to the borrowing undertaken in the year.
  - d. In November 2018 the Treasury Consultants forecast that the Bank Rate would increase from 0.75% to 1.25% during the year. The rate actually remained unchanged at 0.75% during the year until the Covid-19 crisis when, in March 2020, the Bank of England cut the Bank Rate twice in 8 days at emergency meetings, firstly by 0.50% to 0.25% and then down to 0.10% - the lowest Bank Rate ever in the UK. In addition, the Bank added a further £200bn of Quantitative Easing at the second emergency meeting.
  - e. PWLB rates for new borrowing were expected to increase by between 0.20% and 0.40% but rates increased by 0.15% for long-term and up to 0.45% for short-term. The PWLB added 1% to all rates from 9 October 2019. If this increase had not happened then rates would have fallen over the year. Aside from the PWLB addition to rates, the difference in rates for some loan periods between their highest and lowest levels during the year was in line with 2018/19, being 0.30% for some short-term loans but up to 0.64% for longer periods.
  - f. The interest rates for investments remained low during the year and fell in March 2020 with the Bank Rate cuts.
  - g. The Council's investments earned a rate of return of 0.867% during the year and outperformed the benchmark return of 0.634% resulting in additional income to the Council of £51,300.
  - h. All investments were in accordance with the Council's investment policy and no institutions with which investments were made had any difficulty in repaying those investments and interest in full during the year.
  - i. The Council's investment performance is due to undertaking fixed term and notice account investments at interest rates that were above the benchmark with counterparties which have high creditworthiness (the Bank of Scotland and Santander UK) and in accordance with the Council's investment strategy.

- j. The Council undertook a Loan Charges review in 2019/20 which resulted in a one-off £1,411,000 revenue saving in Loan Charge principal repayments for the period to 31/3/2019 and ongoing Loan Charge repayment savings of £400,000 per year from 2019/20 to 2035/36.

5.2 During 2019/20 there was significant economic uncertainty in the UK and around the world. The Covid-19 crisis has caused additional uncertainty with the unknown economic impact (in both size and duration) on the UK and all global economies.

The economic situation continues to be closely monitored.

5.3 The Council's Year End debt position was as follows:

	At 31 March 2019	At 31 March 2020
	£	£
Total Excluding PPP	196,822,590	213,699,487
PPP Debt	62,483,000	60,693,000
Total Including PPP	259,305,590	274,392,487

Further detail is given in the following table:

	At 31 March 2019		At 31 March 2020		Movement 2019/20
	Principal	Rate	Principal	Rate	Principal
	£000		£000		£000
Fixed Rate Funding:					
- PWLB	97,260		114,117		16,857
- Market *	56,000		55,000		(1,000)
	153,260	3.94%	169,117	3.55%	15,857
Variable Rate Funding:					
- PWLB	0		0		0
- Market *	43,400		44,400		1,000
- Temporary #	163		182		19
	43,563	4.93%	44,582	4.86%	1,019
Total Debt (Excl PPP)	196,823	4.16%	213,699	3.82%	16,876
PPP Debt	62,483		60,693		(1,790)
Total Debt (Incl PPP)	259,306		274,392		15,086

\* - Market Loans are shown as variable when they have less than 1 year to go until their next call date. The total value of Market Loans has not changed between financial years, just the split between fixed and variable.

# - Temporary Loans includes funds held by the Council on behalf of the Common Good and Trust Funds and that are to be treated as borrowing for Treasury Management purposes under Scottish Government requirements.

5.4 The Council's cash balances investment position was as follows:

	At 31 March 2019		At 31 March 2020		Movement 2019/20
	Principal	Return	Principal	Return	Principal
	£000		£000		£000
Investments:					
- Fixed Term Deposits	10,000	1.00%	0	0.00%	(10,000)
- Notice Accounts	0	0.60%	10,036	0.25%	10,036
- Deposit Accounts	8,915	0.75%	19,619	0.00%	10,704
Totals	18,915	0.88%	29,655	0.08%	10,740

Investments as at 31 March 2020: £29,655,497

Maximum level of investments in 2019/20: £41,765,824 on 17 September 2019

Minimum level of investments in 2019/20: £7,145,523 on 26 July 2019

Daily average for the year 2019/20: £22,017,234

5.5 2019/20 Outturn Compared to Estimates in 2019/20 Strategy

The 2019/20 outturn compared to the estimates in the 2019/20 strategy:

	2019/20 Estimate	2019/20 Outturn
<u>Borrowing Requirement</u>	£000	£000
New borrowing	5,000	12,000
Alternative financing requirements	0	0
Replacement borrowing	25,000	20,000
TOTAL	30,000	32,000
<u>Prudential/Treasury Management Indicators</u>	£000	£000
Gross external debt including PPP (As at 31 March 2020)	277,456	274,392
Capital financing requirement (As at 31 March 2020)	311,820	302,233
(Under)/over borrowing against CFR	(34,364)	(27,841)
Gross capital expenditure	£000 34,226	£000 25,805
Ratio of financing costs (including PPP) to net revenue stream	14.75%	12.63%
Ratio of net debt (debt and PPP less investments) to net revenue stream	137.0%	124.2%

5.6 The table in paragraph 5.5 above shows that the Council had under borrowed against its capital financing requirement by £27.841m. Under borrowing means that the Council is using cash it already has (e.g. in earmarked reserves and other balances) to cash flow capital expenditure and maturing debt rather than bringing in new funds from borrowing. The level of under borrowing is considered manageable but is kept under review in light of Council capital financing and other funding requirements.

## 5.7 2019/20 Outturn Compared to Limits in 2019/20 Strategy

The 2019/20 outturn compared to limits in the 2019/20 strategy:

### Prudential/Treasury Management Indicators

Authorised limit for external debt

- Borrowing
- Other long term liabilities

Operational boundary for external debt

- Borrowing
- Other long term liabilities

Upper limit on sums invested for periods longer than 364 days (Actual is maximum in period)

Limits on fixed and variable rate borrowing maturing in each period at 31 March 2020 (LOBOs included based on call dates and not maturity dates)

- Under 12 months
- 12 months and within 24 months
- 24 months and within 5 years
- 5 years and within 10 years
- 10 years and within 30 years
- 30 years and within 50 years
- 50 years and within 70 years

### Council Policy Limits

Maximum Percentage of Debt Repayable In Any Year (Actual is as at 31 March 2020 and relates to Financial Year 2077/78)

Maximum Proportion of Debt At Variable Rates (Actual is as at 31 March 2020)

Maximum Percentage of Debt Restructured In Year (Actual is as at 31 March 2020)

2019/20 Limits		2019/20 Outturn	
£000		£000	
249,000		213,699	
63,000		60,693	
312,000		274,392	
£000		£000	
239,000		213,699	
63,000		60,693	
302,000		274,392	
£000		£000	
10,000		0	
Fixed	Var.	Fixed	Var.
45%	35%	7.0%	20.9%
45%	35%	11.7%	0%
45%	35%	7.1%	0%
45%	35%	5.3%	0%
45%	35%	8.2%	0%
45%	35%	21.1%	0%
45%	35%	18.7%	0%
25%		18.7%	
45%		20.9%	
30%		0%	

The forecast Investment Balances for 2019/20 required for “investments” as defined in the Investment Regulations and the actual position at 31 March 2020 are shown in Appendix 1.

## 5.8 The Prudential Code requires that the Council states how interest rate exposure is managed and monitored.

The position in 2019/20 was that all of the Council’s PWLB debt was at fixed rates. The Market debt contained some debt at fixed rates, some small elements at variable rates and some where the rates could change (but none did). The Council’s investments, which were all for less than 1 year, were all variable or regarded as variable under the treasury management rules.

During 2019/20, these interest rate exposures were managed and monitored by the Council through management reports on treasury management that were received and reviewed by the Chief Financial Officer.

- 5.9 The forecast from the Treasury Consultants in the Strategy for the Bank Rate as at 31 March and the latest forecast (produced on 31 March 2020) are:

	Forecast Per 2019/20 Strategy	Actual/ Latest Forecast
2019/20	1.25%	0.10% (Actual)
2020/21	1.50%	0.10% (Forecast)
2021/22	2.00%	0.10% (Forecast)

- 5.10 The Council's Loans Fund Pool Rate for Interest is used to allocate interest charges to the General Fund and reflects the actual cost of the Council's Treasury activities. The rates for the last 5 years (excluding expenses) are as follows:

Year	Loans Fund Pool Rate
2015/16	3.843%
2016/17	3.659%
2017/18	3.557%
2018/19	3.608%
2019/20	3.436%

The Loans Fund Pool Rate for 2019/20 is its lowest level since before Local Government reorganisation.

It is expected that there will be a small increase in the Pool Rate in the medium term.

- 5.11 The Council's investment policy for the year is governed by Scottish Government Investment Regulations and was implemented in the annual investment strategy approved by the Council on 21 February 2019. This policy sets out the approach for choosing investment categories and counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data such as rating outlooks, credit default swaps, bank share prices etc.

All investments in 2019/20 and 2020/21 to date were in accordance with the policy and no institutions with which investments were made had any difficulty in repaying investments and interest in full.

- 5.12 The result of the investment strategy undertaken by the Council in 2019/20 is as follows:

Average Investment	Rate of Return (gross of fees)	Benchmark Return (3 month LIBID un compounded)
£22,017,234	0.867%	0.634%

The Council has outperformed the benchmark by 0.163% resulting in additional income to the Council of £51,300.

## 6.0 OTHER ISSUES

### 6.1 Treasury Consultants Contract

Following a tender process, the Council agreed a new contract with its treasury consultants for an initial 3 year period with 3 one year optional extensions.

## 7.0 LOANS FUND ADVANCES

- 7.1 Where capital expenditure is funded by borrowing (referred to as loans fund advances), the debt financing costs are paid from the Revenue Budget as loan charges comprised of the repayments of debt along with interest and expenses costs on the borrowing.
- 7.2 The Council is required to set out its policy for the repayment of loans fund advances.

For loans fund advances made before 1 April 2016 the policy will be to maintain the practice of previous years and use the Statutory Method (option 1) with annual principal repayments being calculated using the annuity method.

The same method is proposed for loans fund advances made after 1 April 2016 for the permitted 5 year transitional period. In applying the annuity method to new advances in any year, the interest rate used in the annuity calculation will be the Council's loans fund pool rate for the year (including expenses) as rounded up to the nearest 0.01%.

This policy was approved by the Full Council at its meeting on 21 February 2019.

- 7.3 The outstanding loans fund advances (representing capital expenditure still to be repaid from the Revenue Budget) are:

	2019/20
	Actual
	£000
Balance As At 1 April	244,470
Add: Loan Charge Review Adjustment (See Paragraph 7.5)	1,411
	245,881
Add: Advances For The Year	7,057
Less: Repayments For The Year	11,787
Balance As At 31 March	241,151

- 7.4 For the loans fund advances outstanding as at 31 March 2020, the liability to make future repayments (excluding debt interest and expenses) is as follows:

	£000
Year 1	12,299
Years 2-5	32,032
Years 6-10	39,576
Years 11-15	39,172
Years 16-20	35,008
Years 21-25	34,282
Years 26-30	26,985
Years 31-35	12,968
Years 36-40	4,608
Years 41-45	1,197
Years 46-50	1,032
Years 51-55	1,160
Years 56-60	338
Years 61-65	32
Years 66-70	38
Years 71-75	45
Years 76-80	54
Years 81-85	65
Years 86-90	77
Years 91-95	93
Years 96-100	90
TOTAL	241,151

- 7.5 Following Audit Scotland changes to their advice to applying Scottish Government guidance on Loan Charges earlier this year, a review was undertaken of the periods over which previous years' capital expenditure is being written-off to revenue as part of the Loan Charges budget.

The outcome of the review (as reported to the Committee in November 2019) was:

- a. A one-off £1,411,000 revenue saving in Loan Charge principal repayments for the period to 31/3/2019 (the adjustment shown in paragraph 7.3).
- b. Ongoing Loan Charge repayment savings of £400,000 per year from 2019/20 through to 2035/36. After this, the Loan Charge principal repayments will increase as a result of the extension of the write-off periods to bring those periods more in line with the asset lives.

## 8.0 IMPLICATIONS

### Finance

- 8.1 Through the achievement of exceeding the investment benchmark return rate, the Council has benefited from additional returns of £51,300. The Council utilises Treasury Management as part of the overall Financial Strategy. Officers will continue to investigate borrowing and investment opportunities to bring financial benefits to the Council, all within the Treasury Management Policy.

### Legal

- 8.2 None. Any borrowing or lending is done under the Council's legal powers.

### Human Resources

- 8.3 There are no HR implications arising from this report.

### Equalities

- 8.4 There are no equalities implications arising from this report.

#### (a) Equalities

Has an Equality Impact Assessment been carried out?

	YES (see attached appendix)
X	NO – This report does not introduce a new policy, function or strategy or recommend a substantive change to an existing policy, function or strategy. Therefore, no Equality Impact Assessment is required

#### (b) Fairer Scotland Duty

If this report affects or proposes any major strategic decision:-

Has there been active consideration of how this report's recommendations reduce inequalities of outcome?

	YES – A written statement showing how this report's recommendations reduce inequalities of outcome caused by socio-economic disadvantage has been completed.
X	NO



(c) Data Protection

Has a Data Protection Impact Assessment been carried out?

X

YES – This report involves data processing which may result in a high risk to the rights and freedoms of individuals.

NO

**Repopulation**

8.5 There are no repopulation implications arising from this report.

**9.0 CONSULTATIONS**

9.1 This report has been produced based on advice from the Council's treasury consultants (Link Treasury Services Limited).

**10.0 LIST OF BACKGROUND PAPERS**

10.1 CIPFA - Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes – 2017 Edition  
Inverclyde Council – Treasury Management Strategy Statement and Annual Investment Strategy 2019/20-2022/23

**FORECAST OF INVESTMENT BALANCES  
ESTIMATE FOR 2019/20 AND ACTUAL AT 31 MARCH 2020**

Investment Regulation 31 requires the Council to provide forecasts for the level of investments. The estimate for 2019/20 and the actual as at 31 March 2020 are:

	<b>2019/20 Estimate</b>	<b>2019/20 Actual At 31 March 2020</b>
	£000	£000
Cash balances managed in-house		
- At 1 April 2019	25,000	18,915
- At 31 March 2020	19,426	29,655
- Change in year	(5,574)	10,740
- Average daily cash balances	22,213	22,017
Holdings of shares, bonds, units (includes local authority owned company)		
- At 1 April 2019	2	2
- Purchases	0	0
- Sales	0	0
- At 31 March 2020	2	2
Loans to local authority company or other entity to deliver services		
- At 1 April 2019	483	441
- Advances	0	0
- Repayments	42	42
- At 31 March 2020	441	441
Loans made to third parties		
- At 1 April 2019	2,128	2,139
- Advances	0	4
- Repayments	22	26
- At 31 March 2020	2,106	2,117
Total of all investments		
- At 1 April 2019	27,613	21,497
- At 31 March 2020	21,975	32,215
- Change in year	(5,638)	10,718

The movements in the forecast investment balances shown above are due largely to ongoing treasury management activity in accordance with the Council's treasury management strategy or, for loans made to third parties, in accordance with Council decisions made in respect of such loans.

All of the Council's cash balances are managed in-house with no funds managed by external fund managers.

The "holdings of shares, bonds, units (includes authority owned company)" are historic and relate to the Common Good.

The Loans made to third parties includes a £50,000 loan to Shared Interest Society Limited ("Shared Interest") as approved by the Policy & Resources Committee in August 2017. Shared Interest are a company that uses funds invested by individuals and organisations to allow it to provide loans to fair trade businesses around the world.