Report To:	**EXECUTIVE CABINET**
Date:	18 December 2019
Executive Member /Reporting Officer:	Councillor Ryan – Executive Member – Finance and Economic Growth Tom Wilkinson – Assistant Director of Finance
Subject:	**TREASURY MANAGEMENT ACTIVITIES**
Report Summary:	This report provides a mid-year review of the Council's Treasury Management activities for 2019/20, including the borrowing strategy and the investment strategy.
Recommendations:	That the reported treasury activity and performance be noted.
Links to Community Strategy:	The Treasury Management function of the Council underpins the ability to deliver the Council's priorities.
Policy Implications:	In line with Council Policies.
Financial Implications: **(Authorised by the Section 151 Officer)**	The achievement of savings on the cost of financing the Council's debt through repayment, conversion and rescheduling, together with interest earned by investing short term cash surpluses, is a crucial part of the Council's medium term financial strategy. This has to be carefully balanced against the level of risk incurred. The Council held £118.750m of investments as at 30 September 2019 and the investment portfolio yield to date is 1.06% against the London Interbank Bid Rate (LIBID) benchmark of 0.57%. This represents an actual cash return of £0.251m in excess of the benchmark. The Council keeps an average of around 73% of funds in fixed term investments, and the average length of these fixed term investments in 2019/20 to date has been 409 days, compared to 330 days in 2018/19. This has included a small number of investments placed with other Local Authorities for periods in excess of one year in order to achieve an enhanced return.
Legal Implications: **(Authorised by the Borough Solicitor)**	As there is a statutory duty for the Council to set, monitor and comply with its requirements to ensure a balanced budget, sound treasury management is a key tool in managing this process. Demonstration of sound treasury management will in turn provide confidence to the Council that it is complying with its fiduciary duty to the public purse, and in turn allows the Council to better plan and fulfil its key priorities for the coming year. Members should ensure they are fully appraised of **Appendix 1** and the outturn of prudential indicators they are being asked to approve, and the reasons for the same, before making their

decision.

Risk Management: Failure to properly manage and monitor the Council's loans and investments could lead to service failure and loss of public confidence.

Access to Information: The background papers relating to this report can be inspected by contacting Heather Green, Finance Business Partner by:

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1. BACKGROUND

1.1 Cash-flow management is a core element of the Council's financial management activities. The Council operates a balanced budget, which broadly means cash raised during the year will meet cash expenditure. Treasury Management operations firstly ensure that cash flow is adequately planned, with short term surplus funds being invested. The investment strategy priorities are security (i.e. there is a low risk that the counterparty will default on the Council's investment), then liquidity (cash flow needs), and lastly, yield – providing adequate liquidity initially before considering maximising investment return.

1.2 The second main function of the treasury management service is the funding of the Council's capital investment plans, agreed as part of the annual budget setting process and updated throughout the financial year. These capital plans provide a guide to the borrowing need of the Council, essentially this is the long term cash flow planning to ensure the Council can meet its capital spending requirements. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk management or cost reduction objectives.

1.3 Accordingly, treasury management is defined as:

"The management of the local authority's investments and 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. "

2. INTRODUCTION

2.1 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017) was adopted by this Council on 8 February 2012. The primary requirements of the Code are as follows:

i. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

ii. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

iii. Receipt by the full council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, **a Mid-year Review Report** and an Annual Report (stewardship report) to Executive Cabinet covering activities during the previous year.

iv. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

v. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is the Audit Panel.

2.2 This mid-year report has been prepared in compliance with CIPFA's Code of Practice, and covers the following:

- An economic update for the first six months of 2019/20;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's capital expenditure (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;

3. ECONOMIC UPDATE

3.1 The following economic update is provided by the Council's treasury management advisors, Link Asset Services (formally known as Capita Asset Services):

UK: *This first half year has been a time of upheaval on the political front as Theresa May resigned as Prime Minister to be replaced by Boris Johnson on a platform of the UK leaving the EU on or 31 October, with or without a deal. However, in September, his proroguing of Parliament was overturned by the Supreme Court and Parliament carried a bill to delay Brexit until 31 January 2020.*

On 29 October Parliament agreed to hold a general election on 12 December 2019, effectively putting any Brexit talks temporarily on hold. Given these circumstances any interest rate forecasts are subject to material change as the situation evolves. If the UK does soon achieve a deal on Brexit agreed with the EU, including some additional clarification wording on the Irish border backstop, then it is possible that growth could recover relatively quickly. The MPC could then need to address the issue of whether to raise Bank Rate when there is very little slack left in the labour market; this could cause wage inflation to accelerate which would then feed through into general inflation. On the other hand, if there was a no deal Brexit and there was a significant level of disruption to the economy, then growth could weaken even further than currently and the MPC would be likely to cut Bank Rate in order to support growth. However, with Bank Rate still only at 0.75%, it has relatively little room to make a big impact and the MPC would probably suggest that it would be up to the Chancellor to provide help to support growth by way of a fiscal boost by e.g. tax cuts, increases in government departments and services annual expenditure budgets and expenditure on infrastructure projects, to boost the economy.

The first half of 2019/20 has seen UK ***economic growth*** *fall as Brexit uncertainty took a toll. In its Inflation Report of 1 August, the Bank of England was notably downbeat about the outlook for both the UK and major world economies. The MPC meeting of 19 September reemphasised their concern about the downturn in world growth and also expressed concern that the 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 Monetary Policy Committee (MPC) left Bank Rate unchanged at 0.75% throughout 2019, so far, and is expected to hold off on changes until there is some clarity on what is going to happen over Brexit. However, it is also worth noting that the new Prime Minister is making some significant promises on various spending commitments and a relaxation in the austerity programme. This will provide some support to the economy and, conversely, take some pressure off the MPC to cut Bank Rate to support growth.*

As for ***inflation*** *itself, CPI has been hovering around the Bank of England's target of 2% during 2019, but fell to 1.7% in August. It is likely to remain close to 2% over the next two years and so it does not pose any immediate concern to the MPC at the current time. However, if there was a no deal Brexit, inflation could rise towards 4%, primarily as a result of imported inflation on the back of a weakening pound.*

With regard to the ***labour market,*** *despite the contraction in quarterly GDP growth of -0.2%q/q, (+1.3% y/y), in quarter 2, employment continued to rise, but at only a muted rate of 31,000 in the three months to July after having risen by no less than 115,000 in quarter 2 itself: the latter figure, in particular, suggests that firms are preparing to expand output and*

suggests there could be a return to positive growth in quarter 3. Unemployment continued at a 44 year low of 3.8% on the Independent Labour Organisation measure in July and the participation rate of 76.1% achieved a new all-time high. Job vacancies fell for a seventh consecutive month after having previously hit record levels. However, with unemployment continuing to fall, this month by 11,000, employers will still be having difficulty filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation picked up to a high point of 3.9% in June before easing back slightly to 3.8% in July, (3 month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 2.1%. As the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. The latest GDP statistics also included a revision of the savings ratio from 4.1% to 6.4% which provides reassurance that consumers' balance sheets are not over stretched and so will be able to support growth going forward. This would then mean that the MPC will need to consider carefully at what point to take action to raise Bank Rate if there is an agreed Brexit deal, as the recent pick-up in wage costs is consistent with a rise in core services inflation to more than 4% in 2020.

*In the **political arena**, the upcoming general election could result in a potential loosening of monetary policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up although, conversely, a weak international backdrop could provide further support for low yielding government bonds and gilts.*

***USA:** President Trump's massive easing of fiscal policy in 2018 fuelled a temporary boost in consumption in that year which generated an upturn in the rate of strong growth to 2.9% y/y. Growth in 2019 has been falling back after a strong start in quarter 1 at 3.1%, (annualised rate), to 2.0% in quarter 2. Quarter 3 is expected to fall further. The strong growth in employment numbers during 2018 has reversed into a falling trend during 2019, indicating that the economy is cooling, while inflationary pressures are also weakening The Fed finished its series of increases in rates to 2.25 – 2.50% in December 2018. In July 2019, it cut rates by 0.25% as a 'midterm adjustment' but flagged up that this was not to be seen as the start of a series of cuts to ward off a downturn in growth. It also ended its programme of quantitative tightening in August, (reducing its holdings of treasuries etc). It then cut rates again in September to 1.75% - 2.00% and is thought likely to cut another 25 bps in December. Investor confidence has been badly rattled by the progressive ramping up of increases in tariffs President Trump has made on Chinese imports and China has responded with increases in tariffs on American imports. This trade war is seen as depressing US, Chinese and world growth. In the EU, it is also particularly impacting Germany as exports of goods and services are equivalent to 46% of total GDP. It will also impact developing countries dependent on exporting commodities to China.*

***EUROZONE:** Growth has been slowing from +1.8 % during 2018 to around half of that in 2019. Growth was +0.4% q/q (+1.2% y/y) in quarter 1 and then fell to +0.2% q/q (+1.0% y/y) in quarter 2; there appears to be little upside potential to the growth rate in the rest of 2019. German GDP growth fell to -0.1% in quarter 2; industrial production was down 4% y/y in June with car production down 10% y/y. Germany would be particularly vulnerable to a no deal Brexit depressing exports further and if President Trump imposes tariffs on EU produced cars. The European Central Bank (ECB) ended its programme of quantitative easing purchases of debt in December 2018, which meant that the central banks in the US, UK and EU had all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by purchases of debt. However, the downturn in EZ growth in the second half of 2018 and into 2019, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), has prompted the ECB to take new measures to stimulate growth. At its March meeting it said that it expected to leave interest rates at their present levels "at least through the end of 2019", but that was of little help to boosting growth in the near term. Consequently, it announced a third round of*

TLTROs; this provides banks with cheap borrowing every three months from September 2019 until March 2021 which means that, although they will have only a two-year maturity, the Bank is making funds available until 2023, two years later than under its previous policy. As with the last round, the new TLTROs will include an incentive to encourage bank lending, and they will be capped at 30% of a bank's eligible loans. However, since then, the downturn in EZ and world growth has gathered momentum so at its meeting on 12 September, it cut its deposit rate further into negative territory, from -0.4% to -0.5%, and announced a resumption of quantitative easing purchases of debt. It also increased the maturity of the third round of TLTROs from two to three years. However, it is doubtful whether this loosening of monetary policy will have much impact on growth and unsurprisingly, the ECB stated that governments will need to help stimulate growth by fiscal policy. On the political front, Austria, Spain and Italy are in the throes of forming coalition governments with some unlikely combinations of parties i.e. this raises questions around their likely endurance. The recent results of two German state elections will put further pressure on the frail German CDU/SDP coalition government.

CHINA: *Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems. Progress also still needs to be made to eliminate excess industrial capacity and to switch investment from property construction and infrastructure to consumer goods production. The trade war with the US does not appear currently to have had a significant effect on GDP growth as some of the impact of tariffs has been offset by falls in the exchange rate and by transhipping exports through other countries, rather than directly to the US.*

JAPAN: *Japan has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.*

WORLD GROWTH: *The trade war between the US and China is a major concern to financial markets and is depressing worldwide growth, as any downturn in China will spill over into impacting countries supplying raw materials to China. Concerns are focused on the synchronised general weakening of growth in the major economies of the world compounded by fears that there could even be a recession looming up in the US, though this is probably overblown. These concerns have resulted in government bond yields in the developed world falling significantly during 2019. If there were a major worldwide downturn in growth, central banks in most of the major economies will have limited ammunition available, in terms of monetary policy measures, when rates are already very low in most countries, (apart from the US), and there are concerns about how much distortion of financial markets has already occurred with the current levels of quantitative easing purchases of debt by central banks. The latest PMI survey statistics of economic health for the US, UK, EU and China have all been sub 50 which gives a forward indication of a downturn in growth; this confirms investor sentiment that the outlook for growth during the rest of this financial year is weak.*

3.2 Link Asset Service's view on the outlook for the remainder of 2019/20 is as follows:-

What we have seen during the last half year is a near halving of longer term PWLB rates to completely unprecedented historic low levels. There is though, an expectation that financial markets have gone too far in their fears about the degree of the downturn in US and world growth. If, as expected, the US only suffers a mild downturn in growth, bond markets in the US are likely to sell off and that would be expected to put upward pressure on bond yields, not only in the US, but due to a correlation between US treasuries and UK gilts, which at various times has been strong but at other times weaker, in the UK. However, the timing of this and how strong the correlation is likely to be is very difficult to forecast with any degree of confidence.

On 9 October 2019 the PWLB announced an increase in PWLB rates. This is discussed in more detail in section 7, below.

One potential danger that may be lurking in investor minds is that Japan has become mired in a twenty year bog of failing to get economic growth and inflation up off the floor, despite a combination of massive monetary and fiscal stimulus by both the central bank and government. Investors could be fretting that this condition might become contagious.

Another danger is that unconventional monetary policy post 2008, (ultra-low interest rates plus quantitative easing), may end up doing more harm than good through prolonged use. Low interest rates have encouraged a debt fuelled boom which now makes it harder for economies to raise interest rates. Negative interest rates could damage the profitability of commercial banks and so impair their ability to lend and / or push them into riskier lending. Banks could also end up holding large amounts of their government's bonds and so create a potential doom loop. (A doom loop would occur where the credit rating of the debt of a nation was downgraded which would cause bond prices to fall, causing losses on debt portfolios held by banks and insurers, so reducing their capital and forcing them to sell bonds – which, in turn, would cause further falls in their prices etc.). In addition, the financial viability of pension funds could be damaged by low yields on holdings of bonds.

The balance of risks to the UK

- *The overall balance of risks to economic growth in the UK is probably to the downside due to the weight of all the uncertainties over Brexit, as well as a softening global economic picture.*

- *The balance of risks to increases in Bank Rate and shorter term PWLB rates are broadly similarly to the downside.*

  One risk that is both an upside and downside risk is that all central banks are now working in very different economic conditions than before the 2008 financial crash. There has been a major increase in consumer and other debt due to the exceptionally low levels of borrowing rates that have prevailed for eleven years since 2008. This means that the neutral rate of interest in an economy, (i.e. the rate that is neither expansionary nor deflationary), is difficult to determine definitively in this new environment, although central banks have made statements that they expect it to be much lower than before 2008. Central banks could, therefore, over or under-do increases in central interest rates.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- *Brexit – if it were to cause significant economic disruption and a major downturn in the rate of growth.*

- *Bank of England takes action too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.*

- *A resurgence of the Eurozone sovereign debt crisis. In 2018, Italy was a major concern due to having a populist coalition government which made a lot of anti-austerity and anti-EU noise. However, in September 2019 there was a major change in the coalition governing Italy which has brought to power a much more EU friendly government; this has eased the pressure on Italian bonds. Only time will tell whether this new unlikely alliance of two very different parties will endure.*

- *Weak capitalisation of some **European banks**, particularly Italian banks.*

- ***German minority government.*** *In the German general election of September 2017, Angela Merkel's CDU party was left in a vulnerable minority position dependent on the fractious support of the SPD party, as a result of the rise in popularity of the anti-immigration AfD party. Then in October 2018, the results of the Bavarian and Hesse state elections radically undermined the SPD party and showed a sharp fall in support for the CDU. As a result, the SPD had a major internal debate as to whether it could continue to support a coalition that is so damaging to its electoral popularity. After the result of the Hesse state election, Angela Merkel announced that she would not stand for re-election as CDU party leader at her party's convention in December 2018. However, this makes little practical difference as she has continued as Chancellor, though more recently concerns have arisen over her health.*

- ***Other minority EU governments.*** *Austria, Sweden, Spain, Portugal, Netherlands and Belgium all have vulnerable minority governments dependent on coalitions which could prove fragile.*

- ***Italy, Austria, the Czech Republic and Hungary*** *now form a strongly anti-immigration bloc within the EU. There has also been rising anti-immigration sentiment in Germany and France.*

- *There are concerns around the level of* ***US corporate debt*** *which has swollen massively during the period of low borrowing rates in order to finance mergers and acquisitions. This has resulted in the debt of many large corporations being downgraded to a BBB credit rating, close to junk status. Indeed, 48% of total investment grade corporate debt is rated at BBB. If such corporations fail to generate profits and cash flow to reduce their debt levels as expected, this could tip their debt into junk ratings which will increase their cost of financing and further negatively impact profits and cash flow.*

- ***Geopolitical risks,*** *for example in North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.*

Upside risks to current forecasts for UK gilt yields and PWLB rates

- ***Brexit –*** *if agreement was reached all round that removed all threats of economic and political disruption between the EU and the UK.*

- ***The Bank of England*** *is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.*

- ***UK inflation,*** *whether domestically generated or imported, returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.*

3.3 Link Asset Service's view on the anticipated future movement in interest rates is shown below. This forecast includes the increase in margin over gilt yields of 100bps introduced on 9 October 2019.

Link Asset Services Interest Rate View	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25
3 Month LIBID	0.70	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20
6 Month LIBID	0.80	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40
12 Month LIBID	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60
5yr PWLB Rate	2.30	2.50	2.60	2.70	2.70	2.80	2.90	3.00	3.00	3.10
10yr PWLB Rate	2.60	2.80	2.90	3.00	3.00	3.10	3.20	3.30	3.30	3.40
25yr PWLB Rate	3.30	3.40	3.50	3.60	3.70	3.70	3.80	3.90	4.00	4.00
50yr PWLB Rate	3.20	3.30	3.40	3.50	3.60	3.60	3.70	3.80	3.90	3.90

4. TREASURY MANAGEMENT STRATEGY AND ANNUAL INVESTMENT STRATEGY UPDATE

4.1 The Treasury Management Strategy Statement (TMSS) for 2019/20 was approved by the Council on 13 February 2019 as part of the Budget Report.

4.2 There are no required policy changes to the TMSS; the details in this report update the position in the light of the current economic position and budgetary changes already approved.

4.3 In recent years the Council has moved to a more diverse portfolio involving more foreign banks and more longer-duration investments in order to achieve an enhanced return in the current low interest rate environment. All counterparties used have been selected on the basis that they are highly rated and meet the criteria set out in the Council's Treasury Management Strategy.

5. THE COUNCIL'S CAPITAL POSITION (PRUDENTIAL INDICATORS)

5.1 The Prudential Indicators are reported on a quarterly basis as part of the Capital Monitoring process. The Prudential Indicators show the current position against the Prudential Indicator limits initially set as part of the 2019/20 Budget Report.

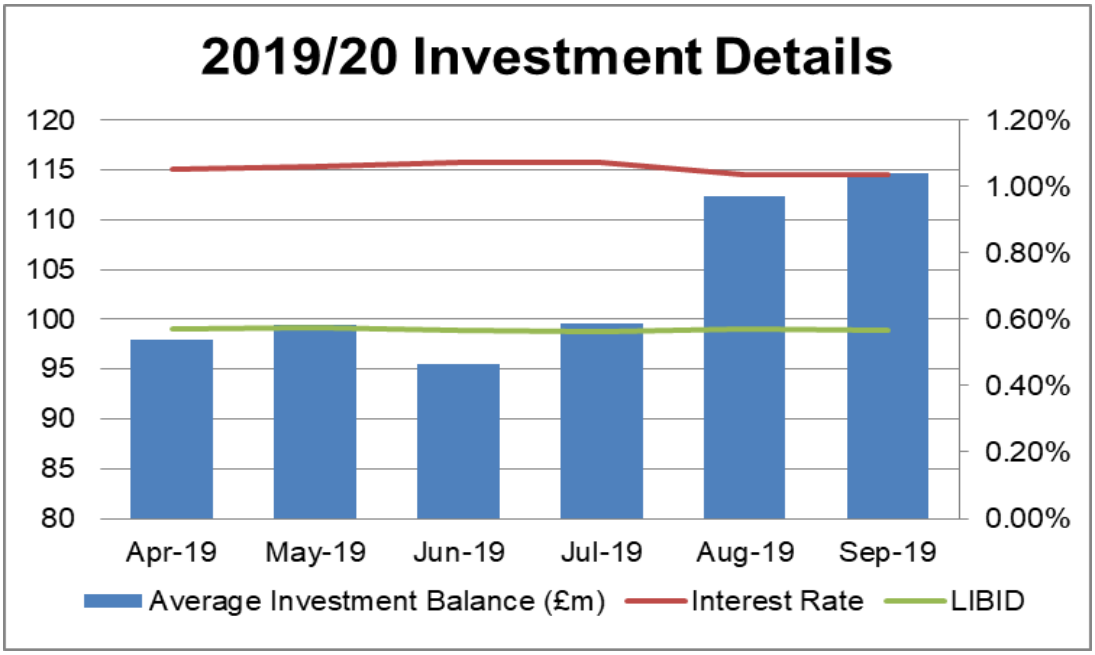
5.2 The indicators are updated from the Capital Programme as at 30 September 2019, showing the Council's capital expenditure plans and how these plans are being financed. Any changes in the capital expenditure plans will impact of the on the prudential indicators and the underlying need to borrow.

5.3 The current prudential indicator position is shown as **Appendix 1** of this report. All the indicators are within the set limits showing that the Council's borrowing strategy remains a prudent one.

6. INVESTMENT PORTFOLIO 2019/20

6.1 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 Section 3, 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 Bank of England Base Rate. The continuing potential for a re-emergence of a Eurozone sovereign debt crisis, and its impact on banks, prompts a low risk strategy. Given this risk environment, investment returns are likely to remain low.

6.2 The Council held £118.750m of investments as at 30 September 2019, with an investment portfolio yield to date of 1.06% against LIBID of 0.57%. At 31 March 2019 the portfolio consisted of £105.300m of investments. The movement is largely in relation to the £30m of borrowing taken up in August less the capital investment to date (£15m as at 30 September). The below graph illustrates the change in investment balances over time along with the change in interest earned and the LIBID benchmark:



6.3 The portfolio as at 30 September 2019 was as follows:

Investment Type	Total Invested	Weighted Average Duration	Weighted Average Interest Rate
	(£m)	(days)	(%)
Money Market Funds	17.250	n/a (overnight)	0.74
Banks (fixed term)	5.000	365	1.10
Banks (notice)	25.000	112	0.97
Local Authorities	71.500	486	1.11
Total	**118.750**	**221**	**1.03**

6.4 As outlined in paragraph 4.3, above, this return has largely been earned due to an increased number of longer-duration investments. This has included a small number of investments placed with other Local Authorities for periods in excess of one year in order to achieve an enhanced return. The average fixed term investment placed by the Council in 2019/20 to date has been 409 days, compared to 330 days in 2018/19. In the first six months of the year an average of £76m (or 73% of total available funds) has been in fixed investments, with the remainder placed on notice or in instant access funds.

6.5 The Assistant Director of Finance confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2019/20.

6.6 The Council's projections as at September 2019/20 show that external loans will incur interest charges of £5.763m and £0.200m will be paid to various Council funds such as the Insurance Fund. Investment income to be earned during the year is estimated to be £2.000m, which will reduce these costs to give a net interest charge budget of £3.763m.

6.7 As outlined in the Treasury Management Strategy, the Council uses the Link Asset Services creditworthiness service to inform counterparty selection.

6.8 The Link Asset Services' creditworthiness service uses a wider array of information than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

6.9 Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

6.10 All credit ratings will be monitored regularly. The Council is alerted to changes to ratings of all three agencies through its use of the Link Asset Services' creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

6.11 Sole reliance will not be placed on the use of this external service. In addition the Council will also use market data and market information, and information on any external support for banks to help support its decision making process.

7. BORROWING

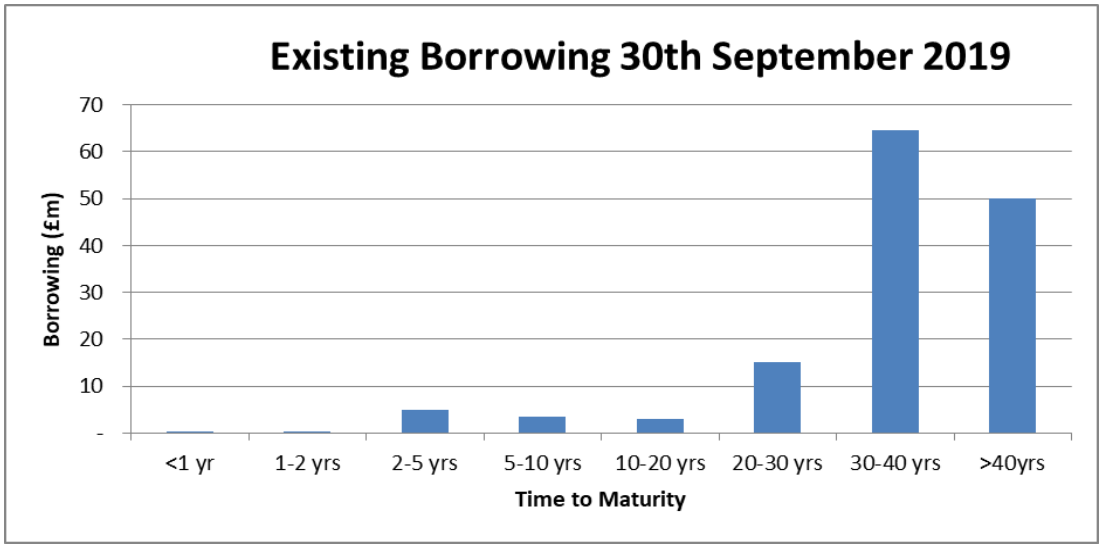
7.1 In August 2019 the Council borrowed £30m (in two tranches of £15m) from the PWLB. This was done during a period of historically low interest rates being offered by the PWLB and has enabled the Council to lock in a significant proportion of funding for Capital Investment at these low rates over the long term.

7.2 On 9 October 2019 the Treasury and PWLB announced an increase in the margin over gilt yields of 100bps on top of the previous margin of 80 bps, which the Council has paid prior to this date for new borrowing from the PWLB. There was no prior warning that this would happen and it now means that every local authority has to fundamentally reassess how to finance their external borrowing needs and the financial viability of capital projects in their capital programme due to this unexpected increase in the cost of borrowing. Representations are going to be made to HM Treasury to suggest that areas of capital expenditure that the Government are keen to see move forward e.g. housing, should not be subject to such a large increase in borrowing.

7.3 Whereas the Council has previously relied on the PWLB as a major source of funding, it now has to fundamentally reconsider alternative cheaper sources of borrowing. At the current time, this is a developmental area as this event has also taken the financial services industry by surprise. There is an expectation that various financial institutions will enter the market or make products available to local authorities.

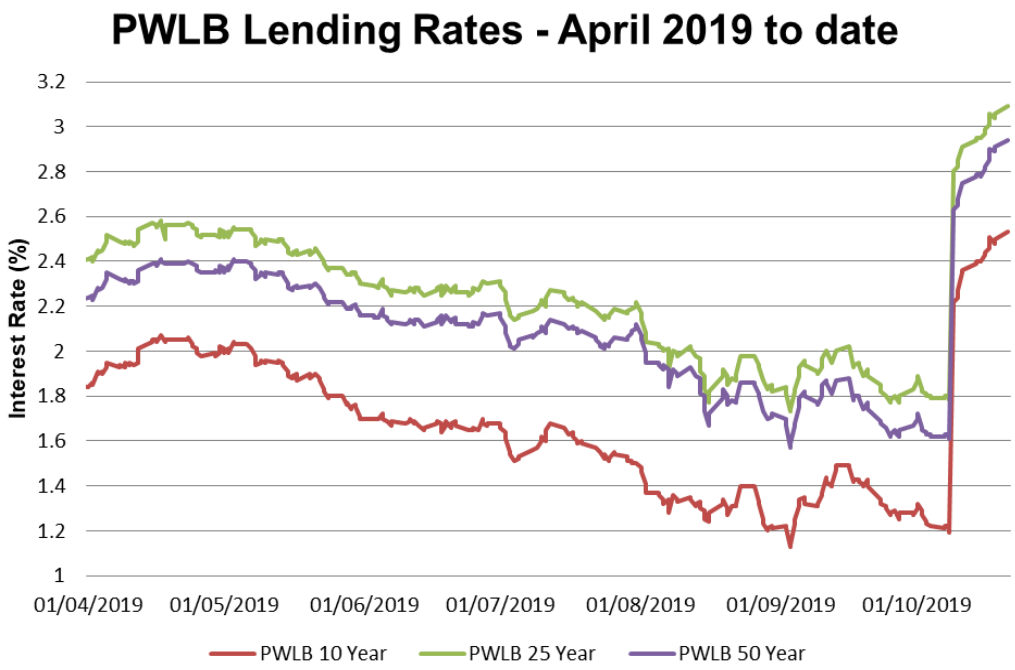
7.4 It is possible that the Municipal Bond Agency will be offering loans to local authorities in the future. The Council may make use of this new source of borrowing as and when appropriate.

7.5 As at 30 September 2019 the Council's total borrowing is £141.531m. The maturity profile is as follows:



7.6 The Council's capital financing requirement (CFR) at 31 March 2019 is £182.611m. 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 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.

7.7 The Council had an outstanding borrowing requirement of £69.548m at 31 March 2019. Initially this was estimated to decrease to £64.852m at 31 March 2019. However, following the £30m of borrowing has taken up in August 2019, this estimate has since been reduced to £34.852m. The remaining outstanding borrowing requirement has been funded from internal balances on a temporary basis and has the impact of reducing the level of the Council's investment balances. This continues to be a prudent and cost effective approach in the current economic climate.



7.8 The table above shows the movement in Public Works Loan Board borrowing rates in 2019/20.

8. MINIMUM REVENUE PROVISION

8.1 The amount of long-term debt that the Council may have is governed by the Prudential Limits set by the Council at the start of the financial year. This is based on the amount of borrowing which the Council has deemed to be prudent. It also allows for advance borrowing for future years' capital expenditure.

8.2 The Council must also allow for repayment of the debt, by way of the Minimum Revenue Provision (MRP). This is the minimum amount that the Council must set aside annually. The Local Authority (Capital Finance and Accounting) Regulations 2008 revised the previous detailed regulations and introduced a duty that an authority calculates an amount of MRP which it considered prudent, although the 2008 Regulations do not define "prudent provision", they provide guidance to authorities on how they should interpret this.

8.3 In 2015/16 the Council's MRP policy was revised from the previous practice (4% of the capital finance requirement on a reducing balance basis) to a straight line method of 2% of the 2015/16 capital financing requirement over a period of 50 years.

8.4 Any new prudential borrowing taken up will be provided for within the MRP calculation based upon the expected useful life of the asset or by an alternative approach deemed appropriate to the expenditure in question. This will continue to be reviewed on an ongoing basis.

8.5 For any finance leases and any on-balance sheet public finance initiative (PFI) schemes, the MRP charge will be equal to the principal repayment during the year, calculated in accordance with proper practices.

8.6 There will be no MRP charge for any cash backed Local Authority Mortgage Scheme (LAMS) that the Council operates. As for this type of scheme, any future debt liability would be met from the capital receipt arising from the deposit maturing after a 5 year period. Any repossession losses for this type of scheme would be charged to a LAMS reserve.

8.7 The MRP policy was updated as part of the 2018/19 Treasury Management Strategy to clarify the Council's position on loans to third parties. The Council considers an MRP charge is not necessary in respect of any loans made to third parties as the debt liability is covered by the existence of a debtor; typically long term depending on the life of the loan. The only expenditure consequence of a loan for an authority is the interest on its cash shortfall whilst the loan is outstanding, so provision for the principal amount would be over-prudent until such time as the assumption has to be made that the loan will not be repaid.

9. DEBT RESCHEDULING

9.1 Debt rescheduling opportunities have been limited in the current economic climate and consequent structure of interest rates. No debt rescheduling was undertaken during the first six months of 2019/20.

10. GREATER MANCHESTER METROPOLITAN DEBT ADMINISTRATION FUND (GMMDAF)

10.1 Tameside Council is the lead council responsible for the administration of the debt of the former Greater Manchester County Council, on behalf of all ten Greater Manchester Metropolitan Authorities. All expenditure of the fund is shared by the authorities on a population basis.

10.2 Unlike Tameside the GMMDAF incurs no capital expenditure, and therefore the total debt outstanding reduces annually by the amount of debt repaid by the constituent authorities. However, loans are raised to replace those maturing during the year, and for cashflow purposes.

10.3 At 31 March 2019 the fund had the following outstanding debt.

	£m
Public Works Loan Board	48.963
Pre 1974 Transferred Debt	0.129
Temporary Loans / (Investments)	9.105
Other Balances	0.647
Total Debt	58.844

10.4 The fund's borrowing requirement for 2019/20 is estimated to be:-

	£m
Long term debt maturing	
Public Works loan Board	10.000
Other	0.036
	10.036
Less principal repayments	(8.556)
Deficit/ (Surplus) in year	(8.520)

10.5 The surplus in year is a result in timing differences between PWLB repayments and the principal repayments from the districts. It will be used to offset an existing deficit from prior years.

10.6 During 2019/20 it is estimated that the total interest payments will be £3.294m at an average interest rate of 5.60%. This compares with 5.23% in 2018/19.

10.7 No long term borrowing has been taken up in the first six months of 2019/20. However, loans may be taken up for either re-scheduling or borrowing early for future years, if prevailing rates are considered attractive. This is now highly unlikely given the limited remaining life of the Fund.

11. RECOMMENDATIONS

11.1 As set out on the front of the report.

Appendix 1 – Prudential Indicators

Actuals v limits as at 30 September 2019

	Limit	Actual	Amount within limit
	£000s	£000s	£000s
Operational Boundary for External Debt	200,356	111,838	(88,518)
Authorised Limit for External Debt	220,356	111,838	(108,518)

These limits include provision for borrowing in advance of the Council's requirement for future capital expenditure. This may be carried out if it is thought to be financially advantageous to the Council.

	Limit	Actual	Amount within limit
	£000s	£000s	£000s
Upper Limit for fixed	182,611	30,022	(152,589)
Upper Limit for variable	60,870	(88,605)	(149,475)

These limits are in respect of the Council's exposure to the effects of changes in interest rates.

The limits reflect the net amounts of fixed/variable rate debt (i.e. fixed/variable loans less fixed/variable investments).

	Limit	Actual	Amount within limit
	£000s	£000s	£000s
Capital Financing Requirement	182,611	182,611	-

The Capital Financing Requirement (CFR) is aimed to represent the underlying need to borrow for a capital purpose and is calculated from the aggregate of specified items on the balance sheet. The CFR increases by the value of capital expenditure not immediately financed (i.e. borrowing) and is reduced by the annual MRP repayment.

	Limit	Actual	Amount within limit
	£000s	£000s	£000s
Capital expenditure	117,301	15,730	(101,571)

This is the estimate of the total capital expenditure to be incurred.

Gross borrowing and the capital financing requirement	CFR @ 31/03/19 + increase years 1,2,3	Gross borrowing	Amount within limit
	£000s	£000s	£000s
	182,611	111,673	(70,938)

To ensure that medium term debt will only be for capital purposes, the Council will ensure that the gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement (CFR).

Maturity structure for borrowing 2019/20 Fixed rate		
Duration	**Limit**	**Actual**
Under 12 months	0% to 15%	0.24%
12 months and within 24 months	0% to 15%	0.25%
24 months and within 5 years	0% to 30%	3.39%
5 years and within 10 years	0% to 40%	2.51%
10 years and above	50% to 100%	93.60%

These limits set out the amount of fixed rate borrowing maturing in each period expressed as a percentage of total fixed rate borrowing. Future borrowing will normally be for periods in excess of 10 years, although if longer term interest rates become excessive, shorter term borrowing may be used. Given the low current long term interest rates, it's felt it is acceptable to have a long maturity debt profile.