Gateshead Council

REPORT TO CABINET
19 NOVEMBER 2019

Title of report: **Treasury Management – Performance to 30 September 2019**

Report of: **Darren Collins – Strategic Director, Resources and Digital**

Purpose of the Report

1. The purpose of this report is to review Treasury Management performance for the six months to 30 September 2019, covering investments and borrowing. This is consistent with approved performance management arrangements.

Background

2. Cabinet will receive half yearly performance reports on the agreed Treasury Management budget identifying any variances. This report sets out the monitoring position at 30 September 2019.

3. Council agreed the Treasury Policy Statement and Treasury Strategy 2019/20 to 2023/24 which provided a framework for the Strategic Director, Resources and Digital to exercise his delegated powers on 19 March 2019.

4. Council also agreed the original General Fund budget for Treasury Management for 2019/20 on 21 February 2019. This was set at £11.053m.

Proposals

5. The projected outturn for 2019/20 at 30 September 2019 is £9.375m compared to the estimate of £11.053m, an underspend on budget of £1.678m.

6. The Audit and Standards Committee reviewed the Treasury Management performance to 30 September 2019 on 28 October 2019 and raised no comments for submission to Council.

7. It is important that effective budget monitoring and action planning is in place to ensure that spending in 2019/20 is contained within approved budgets as this will contribute to a sustainable financial position for the Council.

Recommendation

8. Cabinet is asked to recommend that Council note the Treasury Management Performance to 30 September 2019; to contribute to sound financial management and the long-term financial sustainability of the Council.

CONTACT: Clare Morton, ext. 3591

Appendix 1

Policy Context

1. The proposals in this report are consistent with Council priorities and in particular they ensure that effective use is made of the Council's resources to ensure a sustainable financial position and support of the framework for achieving the Council's strategic approach 'Making Gateshead a Place Where Everyone Thrives'. The Council recognises there are huge financial pressures on not just Council resources, but those of partners, local businesses and residents. This requires the Council's decision-making to be policy and priority led and driven.

Background

2. The Prudential Code plays a key role in capital finance in local authorities. Local authorities determine their own programmes for capital investment that are central to the delivery of quality public services. The Prudential Code was developed by CIPFA, the Chartered Institute of Public Finance and Accountancy, as a professional code of practice to support local authorities in taking their decisions. Local authorities are required by regulation to have regard to the Prudential Code when carrying out their duties in England and Wales under Part 1 of the Local Government Act 2003.

3. In December 2017 CIPFA issued a revised Treasury Management Code of Practice and a revised Prudential Code (the Code) which represent best practice. The Council fully complies with the Code and this contributes towards achieving good practice.

4. Part 1 of the Local Government Act 2003 specifies the powers of a local authority to borrow for any purpose relevant to its functions under any enactment or for the purposes of the prudent management of its financial affairs. Borrowing is linked to the CIPFA Prudential Code for Capital which sets out a range of prudential and treasury indicators that must be calculated to ensure borrowing is affordable, prudent and sustainable. The Prudential Code refers to the need for a clear and integrated treasury strategy.

5. In addition, under Section 15 of the Local Government Act 2003, authorities are required to have regard to the MHCLG's guidance on Local Government Investments. This document stipulates the requirement for an annual investment strategy to be integrated into the Council's Treasury Strategy.

6. Under Part 4 of the Council's Constitution the Strategic Director, Resources and Digital will produce a Treasury Policy Statement annually, setting out the general policies and objectives of the Council's treasury management function.

7. The Council also provides a treasury management service to the Gateshead Housing Company through a Service Level Agreement.

Mid-Year Performance to 30 September 2019

8. This report sets out the latest position on the 2019/20 Treasury Management budget as at 30 September 2019 and projects interest on borrowing and investment income to the end of the financial year.

9. The projected outturn for 2019/20 at 30 September 2019 is £9.375m compared to the estimate of £11.053m, a projected under spend of £1.678m. The underspend is made up of several elements:

   a) Borrowing costs are lower than budget due to lower levels of borrowing taken in the year to date and at lower rates than estimated due to management of cash flows and reliance on internal borrowing.
   b) Investment interest achieved in the year to date has exceeded budgeted estimates, primarily due to higher rates of return available in the market.
   c) Investment interest received from loans to the Council trading companies is more than anticipated in budgeted estimates.

10. Appendix 2 details the budget for 2019/20 compared to an assessment of the projected outturn for the year.

Consultation

11. The Leader of the Council has been consulted on this report.

Alternative Options

12. There are no alternative options, as the Treasury Management mid-year performance report recommended for approval is required to comply with the policy on delegation, review requirements and reporting arrangements as outlined in the Treasury Policy Statement and Treasury Strategy.

Implications of recommended options

13. **Resources:**

a) Financial Implications - The Strategic Director, Resources and Digital confirms that the financial implications are set out in this report. There are no additional financial implications associated with the report itself.

b) Human Resources Implications - There are no human resources implications arising from this report.

c) Property Implications – There are no property implications arising from this report.

14. **Risk Management Implications**

The Treasury Policy and Treasury Strategy which informs activity in this area were prepared with the primary aim of minimising risk to ensure that the Council's principal sums are safeguarded. Maximising income is considered secondary to this main aim.

15. **Equality and Diversity Implications**

There are no equality and diversity implications arising from this report.

16. **Crime and Disorder Implications**

There are no crime and disorder implications arising from this report.

17. **Sustainability Implications**

There are no sustainability implications arising from this report.

18. **Human Rights Implications**

There are no human rights implications arising from this report.

19. **Area and Ward Implications**

There are no direct area and ward implications arising from this report.

Appendix 2

Mid-Year Report - Performance to 30 September 2019

1. Investment Performance

1.1 The latest projection of gross investment income for 2019/20 based on interest earned to date and expected interest to March 2020 is £0.699m, compared to the original estimate of £0.691m.

1.2 This gross investment interest is adjusted to account for £0.373m interest payable to third parties and interest receivable of £1.995m from various third parties, the most significant of which is Newcastle International Airport. This gives a projected net interest to the General Fund 2019/20 of £2.321m compared to the budget of £2.145m. The current variance to budget is mainly as a result of higher levels of interest received on loans to third parties than anticipated when the 2019/20 budget was set.

2. Rate of Return

2.1 The average rate of return is monitored for each investment type that the Council enters into and these are used to calculate an average rate of return for the Council for the year to date. The current rate of return is 0.97%, which is greater than the original estimate of 0.93%.

2.2 The quarterly LINK Asset Services Investment Benchmarking report assesses both the rate of return and the risk of the counterparty to calculate a weighted average rate of return, which is used for comparison across Local Authorities. In the most recent report received, June 2019, the Council achieved a weighted average rate of return of 1.00% on its investments for Quarter 1 2019/20 which is in excess of the risk adjusted expectations (0.89% to 0.99%) defined in the Benchmarking Report for our Group.

2.3 The rate of return would be expected to decrease during the year as investment balances reduce and current deposits are replaced with shorter, lower yielding deposits.

2.4 It is a 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 impact 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.

3. Brexit and the Economy

3.1 The Bank of England's Monetary Policy Committee (MPC) has left Bank Rate unchanged at 0.75% so far in 2019 due to the ongoing uncertainty over Brexit. In its last meeting on 19 September, the MPC became more dovish as it was more concerned about the outlook for both the global and domestic economies based on an assumption that there is an agreed deal on Brexit, where the suggestion that rates would need to rise at a "gradual pace and to a limited extent" is now also conditional on "some recovery in global growth". Brexit uncertainty has had a dampening effect on UK GDP growth in 2019, especially around mid-year. If there

were a no deal Brexit, then it is likely that there will be a cut or cuts in Bank Rate to help support economic growth

4. Borrowing

4.1 The total borrowing for the Council and the Housing Revenue Account (HRA) as at 30 September 2019 was £665.224m, which was within the operational borrowing limit of £865m. This borrowing is made up of £610.524m Public Works Loans Board (PWLB) loans and £54.7m market loans.

4.2 The Treasury Strategy estimates for the 2019/20 financial year were based on a borrowing requirement of £86.564m. To date this year the Council has taken £10m long term borrowing from the PWLB. The timing of further borrowing will depend on a combination of cash flow requirements to support the capital programme and achieving preferential borrowing rates at the time.

4.3 The current forecast for interest payable on borrowing is allocated to the General Fund and the Housing Revenue Account (HRA) as shown in the following table:

	General Fund	**HRA**
Interest Payable	£11.234m	£13.540m
Average rate of interest	3.29%	4.06%

4.4 This represents a gross saving of £1.906m on the original estimate, of which £1.502m is a saving for the General Fund and £0.404m is for the HRA.

5. PWLB Government Intervention

5.1 The maximum net amount of PWLB loans that can be outstanding at any time is subject to a statutory limit. The Government has legislated to increase the lending limit from £85bn to £95bn.

5.2 HM Treasury advised on 9th October 2019 that they would increase the margin that applies to new loans from the PWLB by 100bps (one percentage point) on top of usual lending terms, with immediate effect.

5.3 The Council have reviewed the increase in rates and estimate the additional interest costs for the remainder of this financial year to be in the region of £0.176m. Additional interest costs for 2020/21 are anticipated to be £1.049m, of which £0.732m relates to General fund.

6. Summary of Mid-Year Performance

6.1 The projected net impact of investment and borrowing activity on the revenue budget in 2019/20 is an underspend of £2.107m, comprising £1.678m General Fund and £0.429m HRA.

General Fund	**Estimate £m**	**Projected Outturn £m**	**Variance £m**
Investments	(2.145)	(2.321)	(0.176)
Borrowing	12.736	11.234	(1.502)
Premia	0.462	0.462	0.000
Net Position	11.053	9.375	(1.678)

6.2 Investment returns are likely to remain relatively low during 2019/20 and beyond and interest rates are expected to be below long term borrowing rates therefore value for money considerations indicate that best value can be obtained by delaying new external borrowing and by using internal cash balances to finance new capital expenditure in the short term.

6.3 The current approach of borrowing internally provides benefits in terms of reduced credit risk, as the Council has less cash invested than if it had gone to the markets and borrowed externally. This means that cash balances and investment returns, are historically low resulting in reduced levels of income, which is significantly outweighed by the savings achieved from avoiding external borrowing. The additional element of interest rate risk will be monitored.