REPORT TO: MORAY COUNCIL ON 2 SEPTEMBER 2020

SUBJECT: REPORT ON TREASURY MANAGEMENT PERFORMANCE AND TREASURY AND CAPITAL INVESTMENT PRUDENTIAL INDICATORS FOR 2019/20

BY: DEPUTE CHIEF EXECUTIVE (ECONOMY, ENVIRONMENT & FINANCE)

1. REASON FOR REPORT

1.1 To provide Council with the annual outturn report on Treasury Management and details of the Council's Prudential Indicators for Treasury Management and Capital Investment for the year ended 31 March 2020.

1.2 This report is submitted to Committee in terms of Sections III B (3) of the Council's Scheme of Administration relating to Treasury Management and the Capital Plan.

2. RECOMMENDATION

2.1 It is recommended that the Council consider and note the Treasury Management Performance and the Council's Treasury Management and Capital Investment Prudential Indicators for 2019/20 as set out in the attached APPENDIX 2.

3. BACKGROUND

3.1 Members have agreed that reports on Treasury Management Performance are submitted twice annually. One report to agree the Treasury Management and Investment Strategies with relevant Performance Indicators and the second report to submit the annual review and actual performance of Treasury Management activities. Quarterly Treasury Management monitoring reports are posted on the Members Portal throughout the year.

3.2 The Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector 2017 (the Code) and the Local Government Investment (Scotland) Regulations 2010. All treasury management activities are carried out in accordance with the Code and regulations.

3.3 The primary requirements of the Code are as follows:

- An approved Treasury Management Policy, which sets out the policies and objectives of the Council's treasury management activities.

- Approved Treasury Management Practices, which set out the manner in which the Council will seek to achieve those policies and objectives.

- An annual treasury management strategy report to Council for the year ahead and an annual review report to Council of the previous year.

3.4 The Local Government (Scotland) Act 2003 requires the Council to adopt the CIPFA Prudential Code for Capital Finance in Local Authorities and to produce the prudential indicators set out in the Prudential Code. These indicators are designed to support and record affordable and sustainable capital investment and treasury management.

4. TREASURY PERFORMANCE 2019/20

4.1 This annual Treasury Management performance report covers:

- The Economy and Interest Rates 2019/20
- Treasury Management Strategy for 2019/20
- Annual Investment Strategy 2019/20
- Investment Outturn for 2019/20
- Long Term Borrowing and Debt Rescheduling
- Short Term Borrowing
- Prudential Code for Capital Finance in Local Authorities

The Economy and Interest Rates 2019/20

4.2 During 2019/20, oil prices peaked at $67.31 a barrel in December 2019. Since then, the Covid-19 pandemic has seen a major slump in prices reaching $32.01 per barrel in March 2020, and falling further in April. Prices are starting to recover as lockdown restrictions begin to lift.

4.3 UK Consumer Price Inflation (CPI) for March 2020 was up 1.5% year-on-year, broadly in line with the Bank of England's Inflation Report. The labour market data for the three months to March 2020 showed that the employment rate was at a record high of 76.6%, while the unemployment rate was 3.9%. The growth rate in the rate of pay had been rising steadily but the same three month period saw this slow to 2.7% for regular pay. Once adjusted for inflation, real wages were up 1.0%. The above figures are before the current pandemic. The figures since then have shown a slight decrease in the employment rate but the real impact of the pandemic will likely not be known until the end of the furlough scheme introduced by the UK Government. The growth rate for pay has also decreased and did not increase faster than inflation in the three months to June 2020.

4.4 During 2019, quarterly growth in GDP slowed to between 0.2% and 0.3% on average with the construction sector and production output both seeing falls. Annual GDP growth was 1.1%, down from 1.4 in the previous year.

4.5 Interest rates were at 0.75% for the majority of 2019/20. However, in response to the Covid-19 pandemic, and in an attempt to help the economy, rates were cut in March 2020, first to 0.25% and then further to 0.1%, where it has since remained. The Governor of the Bank of England has said that he cannot see an immediate need to cut interest rates to negative levels but that it was part of the Bank's "toolbox".

4.6 Both globally and domestically, the Covid-19 is having a major impact on the countries around the world. Some countries have seen spikes which has raised the prospect of a so-called "second wave" and talk of the re-imposition of lock down restrictions. The IMF has forecasted the UK economy to contract by 10% this year, with 5% forecasted for the global growth forecast. All 16 countries that the IMF provides forecasts for were forecast to decline, with the exception of China, whose economy is expected to grow by 1%.

4.7 Considerable uncertainty also still surrounds the UK's departure from the EU. It is still unknown if a deal can be reached between the UK and the other 27 Member States prior to our leaving date of 31st December 2020. It is hoped that a deal can be reached by October in order for that to be approved at the EU meeting that month. Undoubtedly, this uncertainty is still having an impact on the economy.

2019/20 Treasury Management Strategy

4.8 The Treasury Management Strategy, incorporating the Annual Investment Strategy, was approved by the Council at its meeting on 27 February 2019 (paragraph 5 of the minute refers).

4.9 The Council's main objective when borrowing is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which the funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

4.10 Given the significant cuts to local government funding, the Council's borrowing strategy continued to address the key issues of affordability without compromising the longer term stability of the debt portfolio. With short-term interest rates much lower than long-term rates, it was more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead. By adopting this approach, the Council is able to reduce net borrowing costs and reduce overall treasury risk.

4.11 The Public Loans Works Board (PWLB) is the Council's preferred source of long-term borrowing given the transparency and control that its facilities continue to provide.

Annual Investment Strategy

4.12 The Council's primary principle when investing is the security of capital and liquidity of investments. The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. It is considered prudent to only invest with highly credited UK financial institutions that have a long-term credit rating of BBB+ or higher.

4.13 The Council's creditworthiness policy has been formulated after consultation with Arlingclose, the Council's treasury advisers. The Chief Financial Officer maintains a counterparty list in compliance with the minimum criteria approved by Full Council on 27 February 2019 (para 5 refers) and any revision to the criteria is submitted to Council for approval as necessary.

4.14 All credit ratings are monitored daily and the Counterparty list is amended to reflect any changes.

Investment Outturn for 2019/20

4.15 The Council manages its investments in-house and invests with the institutions listed on the Council's approved Counterparty list.

4.16 The table below shows the overall investment undertaken by the Council during 2019/20:

	Total Sum Deposited (£m)	**Average Rate (%)**
Approved Financial Institutions	67,300	0.71
Council's Bankers	219,664	0.61
TOTAL	**286,964**	**0.66**

The above figures are cumulative and the actual amounts invested at any one time ranged from £7.70 million to £35.35 million.

4.17 The average rate of interest earned on investments during the year was 0.66%, compared to the average 7 day London Inter Bank Bid Rate (LIBID) of 0.67%.

4.18 As at 31 March 2020, the following balance was invested:

Counterparty	**Investment**	**Amount (£m)**	**Interest Rate (%)**
Bank of Scotland	Call Account	1.528	0.00
Aberdeen Standard	Money Market Fund	5.000	0.48
Federated	Money Market Fund	5.000	0.41
Blackrock	Money Market Fund	5.000	0.37
Insight	Money Market Fund	2.000	0.27
		18.528	**0.30**

Long Term Borrowing and Debt Rescheduling

4.19 The Council's long term external debt position at 31 March 2020 compared with the position at the end of the last financial year was as follows:

	31 March 2019			31 March 2020		
	Actual (£000)	**Rate (%)**	**Average Life (years)**	**Actual (£000)**	**Rate (%)**	**Average Life (years)**
Fixed Rate Funding – PWLB	146,253	4.82	19.40	145,062	4.82	18.27
Fixed Rate Funding – Market	33,400	4.68	54.82	33,400	4.68	53.82
Variable Rate Funding – PWLB	-	-	-	-	-	-
Variable Rate Funding – Market	-	-	-	-	-	-
TOTAL DEBT	**161,203**	**4.80**		**178,462**	**4.75**	

4.20 The Council has been maintaining an under borrowed position which means that the capital borrowing need (Capital Financing Requirement) has not been fully funded with loan debt. Cash supporting the Council's reserves, balances and cash flows has been used as a temporary measure to offset the need to borrow.

4.21 The strategy of effectively delaying new long term borrowing by utilising internal and temporary borrowing has served well at a time when comparatively cheaper temporary borrowing from other local authorities is readily available, counterparties meeting the Council's investment criteria are limited, and historically low investment returns give rise to potentially significant carrying costs for new long-term borrowing.

4.22 To avoid having too large a percentage of short-term debt (i.e. repayable in less than 12 months) compared to the overall debt portfolio, advantage was taken of historically low interest rates to borrow the following long term loans for the Public Works Loans Board (PWLB):

Amount (£)	Rate (%)	Term (years)	Repayment Type
5,000,000	1.02	12	EIP*

*The loan will be paid by equal annual instalments (EIP) over the period of the loan.

4.23 No debt rescheduling was undertaken during the year as the differential between PWLB new borrowing rates and PWLB premature repayment rates made rescheduling unviable.

4.24 CIPFA published revised editions of the Treasury Management and Prudential Codes in December 2017. The required changes from the 2011 Codes have been incorporated into Treasury Management strategies and monitoring reports.

Short Term Borrowing

4.25 During the year, twenty two new temporary loans totalling £73.5m were borrowed from other UK local authorities. A table detailing the short term loans outstanding at 31 March 2020 can be found at **APPENDIX 1.**

The Prudential Code for Capital Finance in Local Authorities

4.26 The Local Government (Scotland) Act 2003 requires the Council to undertake its treasury activities with regard to the Prudential Code for Capital Finance in Local Authorities.

4.27 The Code requires the Council to produce mandatory indicators aimed at assisting members in ensuring that proposed capital investment levels and treasury management decisions satisfy the key requirements of affordability, prudence and sustainability. The Prudential Indicators for 2019/20 were approved at Full Council on 27 February 2019 (paragraph 5 of the minute refers). There were no breaches of these indicators during 2019/20. Performance against key indicators is shown in the **APPENDIX 2.**

5. <u>SUMMARY OF IMPLICATIONS</u>

(a) Corporate Plan and 10 Year Plan (Local Outcomes Improvement Plan (LOIP))
None arising specifically from this report.

(b) Policy and Legal
The Local Government (Scotland) Act 2003 provides the power to borrow and invest as well as providing controls and limits on these activities.

The Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector which details best practice The Local Government Investment (Scotland) Regulations 2010.

All Treasury Management activities are carried out in accordance with the Code and Regulations.

(c) Financial implications
The financial implications are highlighted within the report and the attached **APPENDIX 2**.

(d) Risk Implications
The Council is aware of the risks of passive management of the treasury portfolio and, with the support of the Council's treasury advisers, will proactively manage its investments and debt over the year.

(e) Staffing Implications
There are no staffing implications arising directly from this report

(f) Property
There are no property implications arising directly from this report.

(g) Equalities/Socio Economic Impact
There are no equalities issues arising from this report

(h) Consultations
This report has been produced in consultation with Arlingclose Limited, the Council's Treasury Advisers.

6. CONCLUSION

6.1 The Council's requirements for funds continues to be managed in accordance with the agreed Treasury Management Strategy Statement. All treasury management and capital investment activities have been undertaken with the limits set by the Prudential Code Performance Indicators for 2019/20.

Author of Report: Laurie Milne, Senior Accountant
Background Papers: Various working papers held within Financial Services.
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