Appendix A

TREASURY MANAGEMENT INTERIM REPORT 2018/19

INTRODUCTION

1. The CIPFA Code of Practice for Treasury Management in Local Authorities has been adopted by the Authority. The Code requires that Treasury Management activities are subject to reports to Members. This report represents the interim report for 2018/19.

2. For each financial year the Authority sets a balanced budget so that cash income raised during the year is sufficient to meet all of its cash expenditure commitments. One of the key functions of the Authority's treasury management activity is to ensure that these cash flows are effectively managed, so that cash is available when it is needed. Surplus cash is invested having regard to risk, liquidity and yield.

3. A further key function of the treasury management activity is to ensure that the Authority has sufficient funds to pay for its capital and other investment plans. These capital plans, which are set out in the Capital Programme, identify the borrowing needs of the Authority over a longer time horizon than the current year. In managing its longer term cash flow requirements for capital expenditure the Authority will take out loans or alternatively use its cash flow surpluses in lieu of external borrowing. This latter practice is referred to as "internal borrowing". In managing its loans, it may at times be advantageous for the Authority to repay or restructure its borrowings to optimise interest payments or achieve a balanced debt portfolio.

4. Having regard to these activities, the Chartered Institute of Public Finance and Accountancy (CIPFA) defines treasury management as:

   "The management of the Council'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."

5. As treasury management decisions involve borrowing and investing substantial sums of money, the Authority is exposed to potentially large financial risks, including the loss of invested funds and the revenue effect of changing interest rates. The identification, control and monitoring of risk are therefore integral elements of treasury management activity.

6. The strategy for the year was identified in the Treasury Management Strategy Statement 2018/19 and was contained within the Budget and Financial Plan report CFO/004/18 approved by the Authority at its meeting on 22nd February, 2018. The strategy covered the following areas:

   (a) prospects for interest rates;
   (b) capital borrowing and debt rescheduling;
   (c) annual investment strategy;
   (d) external debt prudential indicators;
   (e) treasury management prudential indicators.
   (f) performance indicators;
   (g) treasury management advisers

7. The Treasury Management Interim Report considers actual treasury management performance up to September 2018.

3. **Executive Summary** of the key points on performance so far include:

- No new borrowing has been arranged in the year or is expected to be arranged.
- No borrowing has been repaid in the year, but £0.5m is due to be repaid in January 2019.
- Financial Investments at 30 September 2018 stood at £42.6m, with associated income of £0.056m compared to an annual budget target of £0.172m for the year.
- The Bank of England (BOE) base rate was raised to 0.75% in August 2018 after remaining at 0.5% since November 2017.
- Longer term Public Works Loan Board (PWLB) rates have increased during the year by 0.29% from 2.47% at the start of the year to 2.76 % at 30 September 2018.
- Treasury Management activity for 2018/19 has been carried out in compliance with the relevant codes and statutes and within the borrowing and treasury management limits approved by the Authority as part of the budget setting process in March 2018.

PROSPECTS FOR INTEREST RATES

3. At its meeting on 2 August 2018 the Bank of England Monetary Policy Committee (MPC) took the decision to increase the base rate to 0.75%, after holding the rate at 0.5% for the first quarter of 2018/19. Whilst this increase is the second of such in the previous twelve months, it is only the second increase in a decade in which rates have been held at historically low levels as part of the response to the financial crisis of 2008. The previous increase was in November 2017 when rates were increased to 0.5% from 0.25%.

4. The MPC continues to recognise that the economic outlook could be influenced significantly by the response of households, businesses and financial markets to developments related to the process of EU withdrawal (Brexit).

5. In the UK, PWLB interest rates and gilt yields have continued to fluctuate during the year with the underlying trend for longer term loans rising by 0.29 % during the first half of the financial year. The table below shows the spread of interest rates during the first six months of the year.

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.48%	1.87%	2.29%	2.70%	2.45%
Date	01/06/18	29/5/18	20/7/18	20/7/18	29/5/18
High	1.77%	2.19%	2.63%	3.03%	2.84%
Date	19/9/18	25/9/18	25/4/18	25/9/18	25/9/18
30/9/18	1.75%	2.13%	2.53%	2.94%	2.76%
Average	1.66%	2.04%	2.45%	2.84%	2.61%

CAPITAL BORROWINGS AND DEBT RESCHEDULING

6. The borrowing requirement comprises the expected movements in the Capital Financing Requirement and reserves plus any maturing debt which will need to be re-financed. The Authority does not envisage that any new long term borrowing will be required in 2018/19.

7. Current PWLB lending terms have severely constrained the option to generate savings via debt rescheduling. A significant rise in long term interest rates is required before rescheduling of debt is viable. However, interest rate structures are continually monitored for opportunities to generate savings from debt rescheduling. Any rescheduling that takes place will be reported to Members in monitoring reports.

ANNUAL INVESTMENT STRATEGY

8. The investment strategy for 2018/19 set out the priorities as the security of capital and liquidity of investments. Investments are made in accordance with DCLG Guidance and CIPFA Code of Practice. Investments are made in sterling with an institution on the counterparty list and for a maximum of one-year duration.

9. Investments have been made with various counterparties including UK and foreign banks with higher credit ratings, the larger Building Societies, "nationalised" banks and AAA rated money market funds. This diversity has enabled reasonable returns in a low interest rate environment. In the period 1st April to 30 September 2018 the average rate of return achieved on average principal available was 0.81 %. This compares with an average seven day deposit (7 day libid) rate of 0.43 %.

10. The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2018/19 are as follows:

UK Government (including gilts and the DMADF)	Unlimited
UK Local Authorities (each)	Unlimited
Part Nationalised UK banks	£4m
Money Market Funds (AAA rated)	£3m
Enhanced Money Market (Cash) Funds (AAA rated)	£3m
UK Banks and Building Societies (A- or higher rated)	£2m
Foreign banks registered in the UK (A or higher rated)	£2m

11. The Authority had investments of £42.6m as at 30th September 2018 (this included a £27.3m firefighters' pension grant received in July that will be utilised in the year):

ANALYSIS OF INVESTMENTS END OF QUARTER 2 2018/19						
Institution	Credit Rating	MM Fund*	Bank / Other	Building Society	Local Authority	Average Interest
		£	£	£	£	%
Blackrock	AAA	3,000,000				0.66
Deutsche/DGLS/State Street	AAA	500,000				0.63
Federated Investors UK	AAA	3,000,000				0.68
JP Morgan Sterling Liquidity Fund	AAA	2,800,000				0.57
LGIM (Legal & General)	AAA	3,000,000				0.67
Morgan Stanley	AAA	300,000				0.61
Standard Life	AAA	3,000,000				0.65
Close Brothers	A		2,000,000			1.15
Goldman Sachs	A		2,000,000			0.89
Santander UK	A		2,000,000			0.85
Sumitomo/SMBCE	A		2,000,000			0.83
Cumberland BS				1,000,000		0.78
Nationwide B Soc				2,000,000		0.59
Newcastle B Soc				1,000,000		0.93
Nottingham B Soc				1,000,000		0.90
Principality B Soc				1,000,000		0.96
West Bromwich B Soc				1,000,000		0.96
Flintshire CC					1,000,000	0.80
Highland Council					2,000,000	0.96
Lancashire CC					2,000,000	1.05
Salford CC					2,000,000	0.70
Slough BC					3,000,000	0.85
South Cambridgeshire DC					2,000,000	0.75
Totals		**15,600,000**	**8,000,000**	**7,000,000**	**12,000,000**	**0.80**
Total Current Investments					**42,600,000**	

**MM Fund - Money Market Funds -these are funds that spread the risk associated with investments over a wide range of credit worthy institutions.*

EXTERNAL DEBT PRUDENTIAL INDICATORS

10. The external debt indicators of prudence for 2018/19 required by the Prudential Code were set in the strategy as follows:

Authorised limit for external debt:	£74 million
Operational boundary for external debt:	£57 million

Against these limits, the maximum amount of debt that was reached in the period April to September 2018 was £39.1 million.

TREASURY MANAGEMENT PRUDENTIAL INDICATORS

11. The treasury management indicators of prudence for 2018/19 required by the Prudential Code were set in the strategy as follows:

a) Interest Rate Exposures
Upper limit on fixed interest rate exposures: 100%
Upper limit on variable interest rate exposures: 50%

The maximum that was reached in the period April to September 2018 was as follows:

Upper limit on fixed interest rate exposures: 100%
Upper limit on variable interest rate exposures: 0%

b) Maturity Structure of Borrowing
Upper and lower limits for the maturity structure of borrowing were set and the maximum and minimum that was reached for each limit in the period April to September 2018 was as follows: -

Maturity Period	Upper Limit	Lower Limit	Maximum Actual	Minimum Actual
Under 12 months	50%	0%	4%	1%
12 months and within 24 months	50%	0%	2%	0%
24 months and within 5 years	50%	0%	10%	9%
5 years and within 10 years	50%	0%	0%	0%
10 years and above	90%	0%	89%	86%

c) Total principal sums invested for periods longer than 364 days
The limit for investments of longer than 364 days was set at £2 million for 2017/18. No such investments have been placed in the first half of 2017/18.

12. **PERFORMANCE INDICATORS**
The Code of Practice on Treasury Management requires the Authority to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking.

13. The indicators for the treasury function are:

Borrowing – the indicator is the average rate of actual borrowing compared to the average available for the period of borrowing. However, there has been no borrowing in the period April to September 2018.

Investments – Internal returns compared to the 7 day LIBID rate. The return in the period April to September 2018 was 0.38 % above the benchmark.

TREASURY MANAGEMENT ADVISORS

14. The treasury management service is provided to the Authority by Liverpool City Council. The terms of the service are set out in an agreed Service Level Agreement. The Council employs treasury management advisors appointed under a competitive procurement exercise who provide a range of services which include: -

- Technical support on treasury matters, capital finance issues.
- Economic and interest rate analysis.
- Debt services which includes advice on the timing of borrowing.

- Debt rescheduling advice surrounding the existing portfolio.
- Generic investment advice on interest rates, timing and investment instruments.
- Credit ratings/market information service comprising the three main credit rating agencies.

15. Whilst Liverpool City Council and its advisors provide the treasury function, ultimate responsibility for any decision on treasury matters remains with the Authority.

CONCLUSION

16. Treasury Management activity in 2018/19 has been carried out in compliance with the relevant Codes and Statutes and within the borrowing and treasury management limits set by the Authority under the prudential code.