APPENDIX A

TREASURY MANAGEMENT ANNUAL 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 regular reports to Members. This report represents the final report on Treasury Management for 2018/19.

2. The strategy for the year was identified in the Treasury Management Strategy Statement 2018/19. The strategy covers 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 advisors

PROSPECTS FOR INTEREST RATES

3. Investment returns remained low during 2018/19. The expectation for interest rates within the treasury management strategy for 2018/19 was that the Bank Rate would rise from 0.50% to 0.75%. At the start of 2018-19, and after UK GDP growth had proved disappointingly weak in the first few months of 2018, the expectation for the timing of this increase was pushed back from May to August 2018. Investment interest rates were therefore on a gently rising trend in the first half of the year after April, in anticipation that the Monetary Policy Committee (MPC) would raise the Bank Rate in August. This duly happened at the MPC meeting on 2 August 2018. It was not expected that the MPC would raise the Bank Rate again during 2018-19 after August in view of the fact that the UK was entering into a time of major uncertainty with Brexit due in March 2019. Value was therefore sought by placing longer term investments after 2 August where cash balances were sufficient to allow this.

4. Investment rates were little changed during August to October but rose sharply after the MPC meeting of 1 November was unexpectedly hawkish about their perception of building inflationary pressures, particularly from rising wages. However, weak GDP growth data after December, plus increasing concerns generated by Brexit, resulted in investment rates falling back again.

5. Continued uncertainty in the aftermath of the 2008 financial crisis has promoted a cautious approach whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

6. PWLB rates and gilt yields have continued to experience exceptional levels of volatility linked to geo-political, sovereign debt crisis and emerging market developments. Long Term PWLB rates peaked during October 2018 at 2.99% before falling sharply to a low of 2.47% by the close of the financial year

7. The overall structure of interest rates has for some time meant that short term rates have remained lower than long term rates. In this scenario, the strategy has continued to be to reduce investments and borrow for short periods and possibly at variable rates when required. However, this needs careful review to avoid incurring higher borrowing costs in the future when the authority may not be able to avoid new borrowing to finance capital expenditure and/or refinance maturing debt.

CAPITAL BORROWINGS AND DEBT RESCHEDULING

8. 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 did not envisage that any new long term borrowing would be required in 2018/19 and no new borrowing was arranged. Market conditions continued to be unfavourable for any debt rescheduling.

ANNUAL INVESTMENT STRATEGY

9. 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 central government regulations 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.

10. Extreme caution was taken in placing investments to ensure security of funds rather than rate of return. The use of deposit accounts with high rated or nationalised banks and AAA rated money market funds has enabled reasonable returns in a low interest rate environment. The credit ratings and individual limits for each institution to be used by the Authority in 2018/19 are outlined below:

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

The average rate of return achieved on average principal available in 2018/19 was 0.82%. This compares with an average seven day deposit (7 day libid) rate of 0.51%.

11. The Investment Strategy specified that investments are only made with banks with a high credit rating. UK banks must have at least an “A” long term rating for inclusion on the Authority’s counterparty list. The money markets are continually monitored for information regarding the creditworthiness of financial institutions and notifications are received of any changes to credit ratings made by any of the rating agencies. An institution is immediately suspended from the Authority’s list of institutions should any doubt arise about its financial standing regardless of whether its credit rating is downgraded.

EXTERNAL DEBT PRUDENTIAL INDICATORS

12. 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 reached at any time in the financial year 2018/19 was £38.1 million.

13. **Gross borrowing and the CFR** - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Authority should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2017/18) plus the estimates of any additional capital financing requirement for the current (2018/19) and next two financial years. This essentially means that the Authority is not borrowing to support revenue expenditure. This indicator allows the Authority some flexibility to borrow in advance of its immediate capital needs. The table below highlights the Authority's gross borrowing position against the CFR. The Authority has complied with this prudential indicator.

	31 March 2018	**31 March 2019**	**31 March 2019**
	Actual	**Estimate**	**Actual**
	£'m	**£'m**	**£'m**
Capital Financing Requirement	64.3	64.5	58.3
Less: PFI	(18.5)	(18.1)	(18.1)
Less:MRD	(0.3)	(0.3)	(0.3)
Borrowing CFR	**45.5**	**46.1**	**39.9**
Existing Debt Portfolio	38.1	37.6	37.6
Over(-)/Under borrowing	**7.4**	**8.5**	**2.3**
Borrowing as a % of CFR	**83.7%**	**81.6%**	**94.2%**

TREASURY MANAGEMENT PRUDENTIAL INDICATORS

14. 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 financial year 2018/19 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 at any time in the financial year 2018/19 was as follows:

Maturity Period	Upper Limit	Lower Limit	Maximum Actual	Minimum Actual
Under 12 months	50%	0%	2%	1%
12 months and within 24 months	50%	0%	1%	0%
24 months and within 5 years	50%	0%	9%	8%
5 years and within 10 years	50%	0%	0%	0%
10 years and above	90%	0%	90%	89%

c) Total principal sums invested for periods longer than 365 days
The limit for investments of longer than 365 days was set at £2 million for 2018/19. No such investments were placed during 2018/19.

PERFORMANCE INDICATORS

15. 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.

16. The indicators for the treasury function are:

    Borrowing - Average rate of long term borrowing for the year compared to average available. No new long term borrowing was arranged in 2018/19.

    Investments – Internal returns compared to the 7 day LIBID rate. The return in the financial year 2018/19 was 0.31% above the benchmark.

TREASURY MANAGEMENT ADVISORS

17. 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 advisers 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.

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

CONCLUSION

19. 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.