CLACKMANNANSHIRE COUNCIL	THIS PAPER RELATES TO ITEM 15 ON THE AGENDA

Report to: **Council**

Date: **28 June 2018**

Subject: **Annual Treasury Management Report 2017/18**

Report by: **Interim Chief Accountant**

1.0 Purpose

1.1 The purpose of this report is to detail the Treasury Management activities for the Council for 2017/18.

1.2 The Council is required by regulations issued under the Local Government in Scotland Act 2003 to produce an annual review of treasury management activities. This report details the treasury management activities for the Council for 2017/18 and how this compares to the Council's Treasury Management Strategy Statement.

2.0 Recommendations

2.1 It is recommended that the Council note and consider this Annual Report for 2017/18 on the Council's Treasury Management activities.

3.0 Considerations

3.1 This report meets the requirements of the Scottish Government's investment regulations, the CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

3.2 During 2017/18 the minimum requirement was that the following reports should be submitted to Elected Members:

- ➢ an annual treasury management and investment strategy (The Treasury Management Strategy Statement (TMSS) for 2017/18, which included the Annual Investment Strategy was approved by Council on 27th March 2017)
- ➢ a mid-year treasury update report (Treasury Management Update at 30th September 2017 submitted to the Council on 12th December 2017)
- ➢ an annual review following the end of the year describing the activity compared to the strategy (this report).

Regulations place responsibility on members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

3.3 The report covers the following:

- The Economy and Interest Rates
- Interest Rate Forecast
- Investment Outturn for 2017/18
- Borrowing Requirement and Debt
- Borrowing Outturn for 2017/18
- Compliance with Treasury and Prudential Limits

The Economy and Interest Rates

3.4 The economy saw some growth in 2017, but the first quarter of 2018 has been the low. While the outcome of the negotiations on the UK's departure from the EU is not yet known, both the Scottish Fiscal Commission and the Office for Budget Responsibility expect it to have a negative impact on the economy. UK economic growth slowed over quarter 1 2018, but this has been mostly attributed to adverse weather condition and is expected to increase in quarter 2. Inflation remains above the target 2% but this has been mainly due to Brexit, with pass through of falling sterling rates resulting in higher import costs, however forecast predict that this will stabilise and bring inflation nearer 2% as the year progresses. The increase in inflation has also reduced consumer's disposable income and spending power.

3.5 The Monetary Policy Committee (MPC) meeting minutes of 14 September 2017 indicated that Bank Rate would need to rise shortly. The potential bank rate rise was attributed to the CPI inflation of 2.9% in August which was marginally higher than previously forecast and unemployment falling to 4.3%, the lowest level since 1975. CPI inflation peaked at 3.1% in November 2017 as the MPC had forecast and the February 2018 MPC forecast that CPI will be above its target rate of 2% in two years' time. Low unemployment has a significant impact on the capacity in the labour market to support growth in the economy and the MPC's view is that the amount of spare capacity in the economy has also significantly diminished.

Interest Rate Forecast

3.6 The Council's treasury advisors - Link Asset Services, have provided the following interest rate forecast which is in line with the economic outlook set out in paragraphs 3.3 & 3.4 above.

Table1: Investment Forecast provided by Link Asset Management

Quarter Ended	Bank Rate %	PWLB Borrowing Rates (including certainty rate adjustment)		
		5 year	25 year	50 year
March 2018	0.50	1.90	2.80	2.60
June 2018	0.75	2.00	2.90	2.70

Quarter Ended	Bank Rate %	PWLB Borrowing Rates (including certainty rate adjustment)		
Sept 2018	0.75	2.10	3.00	2.80
Dec 2018	1.00	2.10	3.10	2.90
March 2019	1.00	2.20	3.20	3.00
June 2019	1.00	2.30	3.20	3.00
Sept 2019	1.00	2.30	3.30	3.10
Dec 2019	1.25	2.40	3.30	3.10
March 2020	1.25	2.40	3.40	3.20
June 2020	1.25	2.50	3.50	3.30
Sept 2020	1.50	2.50	3.50	3.30
Dec 2020	1.50	2.60	3.60	3.40
March 2021	1.50	2.60	3.60	3.40

3.7 The Bank Rate was increased from 0.25% to 0.5% on 2nd November 2017 by the MPC. Two further increases are expected during 2018/19; June 2018 and Dec 2018, which will increase the rate to 1.00%. A further 2 increases are also expected during 2019/20 and 2020/21 increasing the rate to 1.50% by March 2021.

Investment Outturn for 2017/18

3.8 The Treasury Management Strategy Statement (TMSS) for 2017/18, which includes the Annual Investment Strategy, was approved by the Council on 27th March 2017**.** As at 31st March 2018, the Council held investments of £28.9m made up of £19.7m short-term cash and cash equivalents held with banks and £9.3m investment held mainly in Clackmannanshire Regeneration and Coalsnaughton NHT Project. Appendix 1 shows the analysis of the investment portfolio as at 31st March 2018.

The Council's the treasury indicator and limit for investments for 2017/18 was that the maximum principal sum invested for period greater that 364 days (long-term) was £12m. The approved limits within the Annual Investment Strategy relating to investments were not breached during 2017/18.

3.9 As at 31st March 2018 the Council held immediately available cash balances of £9.6m (£9.8m 2016/17). The immediately available cash balances were reduced for the first six months of the year mainly due to the scheduled repayment of the £3m temporary loan. The average levels of funds available for investment during the period to 31st March 2018 were £17.5m. During the year, two deposits of £5m each were returned to the Council and two £5m month deposits, with lengths of 12 months and 6 months, have been invested.

3.10 Investment rates for three months and longer, increased after the MPC meeting in February, due to the indication that rates would increase more quickly than previously indicated. The benchmark investment returns over the 12 months ending 31st March 2018 are illustrated in the undernoted table:

Table 2: Benchmark Investment Returns 2017/18

Benchmark	Benchmark Return
7 day	0.21%
1 month	0.23%
3 month	0.29%
6 month	0.40%
12 month	0.61%

3.11 The Council's budgeted cash investment return for 2017/18 was 0.25%. The Council achieved an actual investment return of 0.53% (£92k) for the year ended 31st March 2018. This comprised of two £5m, twelve month investments with returns of 0.80% and 0.90% outperforming the 12 month benchmark by 0.19% and 0.29% respectively and a six month investment at 0.75% outperforming the benchmark by 0.35%. A return of 0.17% was achieved on everyday cash balances which was 0.04% less than the benchmark return for 7 day investments. The actual investment return is higher than the budgeted return of 0.25% due to an active review of ongoing available deposit rates and an increase in the bank rate part way through the year. Future opportunities may be available to maximise investment income for the 2018/19 financial year in line with expectations of future increases to interest rates if this is passed onto customers.

Capital Outturn for 2017/18

3.12 The Council's capital expenditure plans are a key driver of treasury management activity. The Treasury Management Strategy Statement (TMSS) for 2017/18 provided estimates of the total capital expenditure, split between General Fund Services and Housing Revenue Account (HRA), for 2017/18 and the following four financial years. The outturn for 2017/18 is as follows:

Table 3: Capital Outturn 2017/18

	1 April 2018 Budget £000	31 March 2018 Actual £000	(Under)/Over Spend £000
General Fund Services	15,634	11,453	(4,181)
Housing Revenue Account	9,940	6,106	(3,834)
Total	**25,574**	**17,559**	**(8,015)**

The underspends are mainly due to slippage in large projects. This will be explored in the budget setting process for future years.

Borrowing Need 2017/18

3.13 Capital expenditure that is not financed by the use of capital receipts, capital grants or directly from revenue, will increase the capital financing requirement of the Council. The calculation of the Capital Financing Requirement is therefore intended to reflect the Council's underlying need to borrow for a capital purposes and it is used as a key measure in treasury management decisions for this reason. Increases in the CFR, as a result of capital expenditure not paid from capital or revenue resources, are offset by the Loan Fund Principal Repayment. This is the amount required to be charged to revenue for previous borrowing and it is charged over the life of the asset.
The CFR is split between the General Fund CFR and the HRA CFR and is shown in the table below.

Table 4: Borrowing Requirement (CFR) 2017/18

	31 March 2017 Actual £000	1 April 2018 Budget £000	31 March 2018 Actual £000
CFR General Fund	120,273	123,640	119,247
CFR HRA	26,729	25,557	25,173
Total CFR	**147,002**	**149,197**	**144,420**

The CFR for 2017/18 has reduced due to slippage in the respective capital programmes. The annual change is a reduction of £2.5m.

Ratio of financing costs to net revenue stream

3.14 The Council is required to make estimates of the ratio of capital financing costs to its net revenue stream i.e. the estimate of total income which will be committed towards meeting future costs of borrowing. The outturn for 2017/18 is as follows

Table 5: Ratio of financing costs to net revenue stream 2017/18

	2017/18 Budget	2017/18 Actual
General Fund	8.09%	8.39%
Housing Revenue Account	16.03%	16.05%

Borrowing Outturn for 2017/18

3.15 Borrowing activity is constrained by the prudential indicators for CFR and gross borrowing and by the authorised limit. The Council needs to ensure that gross debt does not, over the long term, exceed the CFR. An over borrowing position is permissible in the short term to allow for early borrowing for future years but the Council must return to an under borrowed position in future years.

New Borrowing

3.16 During the period to 31st March 2018, the Council repaid a maturing temporary loan of £3.0m.

3.17 The budgeted capital spend was funded from internal borrowing (cash balances) and a 7-year 6-month PWLB loan of £1.071m.

3.18 Repayments of £1.062m were also made in the year toward the Council's PFI and finance lease.

3.19 The Council's external borrowing position as at 31st March 2018 is illustrated in the undernoted table:

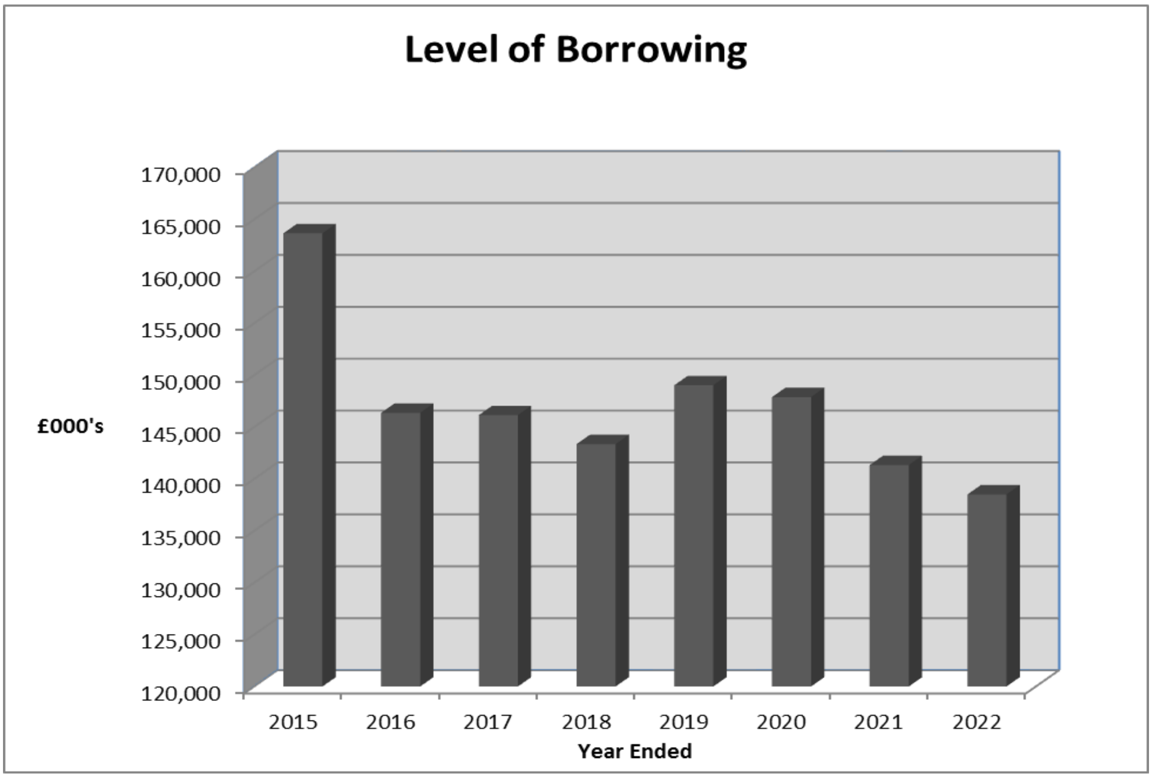
Table 6: External borrowing at 2017/18

	Actual March 2017 £000	**Actual March 2018 £000**
Public Works Loan Board	76,444	77,515
Market Loans	19,300	19,431
LOBO Loans	5,000	5,000
Other long term liabilities	42,404	41,342
Temporary Loans (<1 year)	3,000	0
Total	**146,148**	**143,288**
CFR	**147,002**	**144,420**
(Under)/Over borrowing	**(854)**	**(1,132)**

As at 31st March 2018, the Council is in an under borrowed position. Appendix 2 shows the maturity structure of the PWLB loan, Market loans and LOBO loans and the upper and lowers limits as set out in the TMSS for 2017/18.

3.20 The Capital Programme has been set in line with the Council's strategy to reduce long term debt. The level of borrowing has reduced at the end of 2017/18 and is forecast to increase in 2018/19 and 2019/20 before reducing again from 2020/21 onwards. The increase is due to significant capital projects in these years, including Tullibody South Campus and Kilncraigs final payment. The following chart illustrates this, demonstrating actual and forecast level of debt up to the end of 2021/22. In addition to programme capital spend, repayment profiles of debt maturity, mean there are variations in annual change in debt year on year.

Chart 1: External debt (actual and forecast)



3.21 Overall there is a forecasted reduction in cumulative external debt of 15% between 2015 and 2022, showing that over the longer term the Council is not increasing its level of debt, to finance its capital programme. Repayments towards PFI and finance leases also continue to reduce the Council's overall level of external debt on an annual basis.

Limits for External Debt

3.22 The Council is required to set an authorised limit for external debt which includes external borrowing (gross of investments) and other long term liabilities such as finance lease obligations. The limit provides a maximum figure that the Council could borrow at any given point during each financial year. The Council also set an operational boundary for external debt which is lower than the authorised limit as it is based on an estimate of the most likely level of external borrowing at any point in the year.

Table 5: Authorised Limit for External Debt 2017/18

	2017/18 £000
Authorised Limit for External Debt	162,000
Operational Boundary for External Debt	152,000
Gross External Debt as at 31st March 2018	143,288

The Council did not exceed the authorised limit or the operational boundary during 2017/18 and was £8.7m below the operation boundary as at 31st March 2018.

Borrowing in advance of need

3.23 The Council has not borrowed in advance of need in the year ended 31st March 2018 and has no intention to borrow in advance in 2018/19.

Debt Rescheduling

3.24 Debt rescheduling opportunities have been very limited in the current economic climate given the consequent structure of interest rates which has impacted on PWLB new borrowing rates since October 2010. Consequently no debt rescheduling has been undertaken.

Compliance with Treasury and Prudential Limits

3.25 It is a statutory duty for the Council to determine and keep under review the affordable capital expenditure limits. The Council's Treasury and Prudential Indicators (affordability limits) are included in the approved Treasury Management Strategy Statement.

3.26 During the year the Council has operated within the treasury and prudential indicators set out in the Council's Treasury Management Strategy Statement and in compliance with the Council's Treasury Management Practices. The Prudential and Treasury Indicators are shown at Appendix 2.

4.0 Conclusions

4.1 The Council has complied with its legislative and regulatory requirements.

4.2 Immediately available cash balances were reduced for the first six months of the year mainly due to the repayment of the £3m temporary loan.

4.3 The Council has repaid £1.062m towards PFI and Finance leases

4.4 The Council continues to outperform the benchmark return in interest on investments. Cash balances for 2017/18 were at an average level of c£17.5m which contributes to supporting the Council's capital financing requirement internally.

5.0 Sustainability Implications

5.1 None

6.0 Resource Implications

6.1 Financial Details

6.2 The full financial implications of the recommendations are set out in the report. This includes a reference to full life cycle costs where appropriate.

Yes ☑

6.3 Finance have been consulted and have agreed the financial implications as set out in the report.

Yes ☑

6.4 Staffing

6.5 None

7.0 Exempt Reports

7.1 Is this report exempt? Yes ☐ (please detail the reasons for exemption below)

No ☑

8.0 Declarations

The recommendations contained within this report support or implement our Corporate Priorities and Council Policies.

(1) **Our Priorities** (Please tick ☑)

The area has a positive image and attracts people and businesses	☐
Our communities are more cohesive and inclusive	☐
People are better skilled, trained and ready for learning and employment	☐
Our communities are safer	☐
Vulnerable people and families are supported	☐
Substance misuse and its effects are reduced	☐
Health is improving and health inequalities are reducing	☐
The environment is protected and enhanced for all	☐
The Council is effective, efficient and recognised for excellence	☑

(2) Council Policies (Please detail)

Treasury Management Policy Statement and Practices

9.0 Equalities Impact

9.1 Have you undertaken the required equalities impact assessment to ensure that no groups are adversely affected by the recommendations?

N/A Yes ☐ No ☐

10.0 Legality

10.1 In adopting the recommendations contained in this report, the Council is acting within its legal powers. Yes ☑

11.0 Appendices

11.1 Please list any appendices attached to this report. If there are no appendices, please state "none".

Appendix 1 – Investment Portfolio as at 31st March 2018

Appendix 2 - Prudential and Treasury Indicators as at 31st March 2018

12.0 Background Papers

12.1 Have you used other documents to compile your report? (All documents must be kept available by the author for public inspection for four years from the date of meeting at which the report is considered)

Yes ☑ (please list the documents below) No ☐

Treasury Management Strategy 2017/18 - report to Council March 2017

Author

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Paula Tovey	Interim Chief Accountant	2078

Approved by

NAME	DESIGNATION	SIGNATURE
Stephen Coulter	Head of Resources & Governance	[redacted]
Nikki Bridle	Chief Executive (Acting)	

APPENDIX 1: Investment Portfolio as at 31st March 2018

Borrower	Principal £000	Interest Rate	Start Date	Maturity Date
Bank of Scotland Plc	5,000	0.80%	21/04/17	20/04/18
Bank of Scotland Plc	5,001	0.75%	19/02/18	13/08/18
Bank of Scotland Plc	2,812	0.25%	Instant Access	
Royal Bank of Scotland Plc	6,790	0.15% (balances above £1m)	Instant Access	
Other Accounts	48			
Total Cash and Cash Equivalents	**19,651**			

Short Term Investments	Principal £000
CSBP Developments	0
Total Short Term Investments	**0**

Long Term Investments	Principal £000
CSPB Investments	1
Clackmannanshire Regeneration	4,906
Coalsnaughton NHT Project	4,358
Total Long Term investments	**9,265**

TOTAL INVESTMENTS	**28,916**

APPENDIX 2: Prudential and Treasury Indicators as at 31st March 2018

Treasury Indicators	2017/18 Budget £000	2017/18 Outturn £000
Authorised limit for external debt	162,000	162,000
Operational boundary for external debt	152,000	152,000
Gross external debt*	148,943	143,288
Investments	25,008	28,916
Net borrowing	123,935	114,372

*As at 31st March 2018, Gross external debt consisted of ££102.946m fixed rate borrowing and £41.342m liabilities in relation to the PFI and finance leases

Maturity structure of fixed rate borrowing - upper and lower limits (excluding PFI and Finance Leases)	Upper and Lower Limits	Fixed Rate Borrowing as at 31st March 2018 £000	% of Total Fixed Rate Borrowing
Under 12 months	25% - 0%	5,063	5.0%
12 months to 2 years	25% - 0%	63	0.1%
2 years to 5 years	50% - 0%	3,546	3.5%
5 years to 10 years	75% - 0%	6,769	5.6%
10 years and above	100% - 0%	87,505	85.8%
Total Fixed Rate Borrowing		102,946	100%

APPENDIX 2: Prudential and Treasury Indicators as at 31st March 2018

Prudential Indicators	2017/18 Budget £000	2017/18 Outturn £000
Capital expenditure - General Fund Services	15,634	11,453
Capital expenditure - Housing Revenue Account	9,940	6,106
Capital Financing Requirement (CFR) - General Fund	123,640	119,247
Capital Financing Requirement (CFR) - HRA	25,557	25,173
Annual change in CFR - General Fund	1,121	(1,026)
Annual change in CFR - HRA	(1,165)	(1,556)
In year borrowing requirement	7,225	1,272
Ratio of financing costs to net revenue stream - General Fund	8.09%	8.39%
Ratio of financing costs to net revenue stream - HRA	16.03%	16.05%