Annual Report 2019/20
Treasury Management and Actual Prudential Indicators

1. Introduction

1.1 The Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

- The Local Government in Scotland Act 2003 (the Act), provides the powers to borrow and invest as well as providing controls and limits on this activity. The Act permits the Scottish Ministers to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions were made in 2019/20);

- Statutory Instrument (SSI) 29 of 2004, requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities, and therefore to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services; and the treasury activity with regard to the CIPFA Code of Practice for Treasury Management in Local Authorities; and

- Statutory Instrument (SI) 2016 No 123 requires the Council to document its policy on the prudent repayment of loans fund advances.

1.2 This Council has adopted both the CIPFA Code of Practice for Treasury Management in the Public Sector and the Prudential Code and operates its treasury management service and capital programme in compliance with these Codes and the above requirements. These require that the prime objective of the treasury management activity is the effective management of risk, and that its borrowing activities are undertaken in a prudent, affordable and sustainable basis.

In December 2017, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued a revised Treasury Management Code and a revised Prudential Code.

A particular focus of these revised codes was how to deal with local authority investments which are not treasury type investments e.g. by investing in purchasing property in order to generate income for the Authority at a much higher level than can be attained by treasury investments. One recommendation was that local authorities should produce a new report to members to give a high level summary of the overall capital strategy and to enable members to see how the cash resources of the Authority have been apportioned between treasury and non-treasury investments. A Capital Strategy was reported and approved by Council on 4 March 2020.

1.3 During 2019/20 the minimum reporting requirements were that the Council should receive the following reports:

- an annual treasury strategy in advance of the new financial year (Council 27 March 2019);
- a mid-year treasury update report (Council 30 October 2019); and
- an annual report following the financial year-end describing the activity compared to the strategy (this report).

1.4 This report sets out:

- A summary of the strategy agreed for 2019/20;
- The Council's treasury position at 31 March 2020;
- The main Prudential Indicators and compliance with limits;
- A summary of the economic factors affecting the strategy over 2019/20;
- The Treasury activity during 2019/20;
- Performance indicators set for 2019/20;
- Disclosure regarding the repayment of loan Fund advances for 2019/20; and
- Risk and Performance.

2. A Summary of the Strategy for 2019/20

2.1 **Borrowing** - keeping note of the slightly over-borrowed position of the Council as at 31 March 2019 and the risk within the economic forecast at that time, caution was adopted with the 2019/20 treasury operations. The Section 95 Officer planned to monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances.

2.2 **Investments -** with the economic background at the time, the investment climate had one over-riding risk consideration - counterparty security risk. As a result of the underlying concerns, officers implemented an operational investment strategy which tightened the controls already in place in the approved investment strategy. The Council's investment strategy primary objectives are safeguarding the re-payment of the principal and interest of its investments on time first and ensuring adequate liquidity second – the investment return being a third objective.

2.3 Based on the above, the treasury strategy was to postpone borrowing (by not borrowing in advance of need) and in particular minimise longer term borrowing to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

3. The Council's Treasury Position at 31 March 2020

3.1 During 2019/20, the Strategic Lead – Resources, in line with the Treasury Strategy, managed the debt position with the use of internal funds as well as a mix of short term and long term external borrowing, and the treasury position at 31 March 2020 compared with the previous year was:

Table 1

Treasury position – excluding PPP	**31 March 2020**		**31 March 2019**	
	Principal	**Average Rate**	**Principal**	**Average Rate**
Fixed Interest Rate Debt	£509.678m	2.25%	£441.370m	2.51%
Variable Interest Rate Debt	£0.000m	0.00%	£0.000m	0.00%
Total Debt	**£509.678m**	**2.25%**	**£411.370m**	**2.51%**
Total Investments	**£21.246m**	**0.74%**	**£19.389m**	**0.64%**
Net borrowing position	**£488.432m**		**£421.981m**	

3.2 From the above table, it can be seen that the average interest rate on debt held on 31 March 2020 has reduced from 2.51% to 2.25%. At the same time the average interest rate has increased on the investments held on 31 March 2019 to 2020 from 0.64% to 0.74%.

3.3 The external debt figure included within Table 1 includes both short term and long term debt. The low average interest rate is due to a strategy of using short term borrowing to fund long term capital investment enabling the Council to take advantage of lower interest rates.

3.4 There are four treasury prudential indicators which cover the activity of the treasury function. Complying with these indicators reduces the risk of an adverse movement in interest rates impacting negatively on the Council's overall position:

- Upper limits on variable rate exposure;
- Upper limits on fixed rate exposure;
- Maturity structures of borrowing; and
- Total principal funds invested for greater than 365 days.

3.5 Table 2 shows the actual upper limits set per debt type and maturity as at 31 March 2020.

Table 2

	2019/20 Actual	**2019/20 Indicator**	
Upper limits on variable interest rates	0%	50%	
Upper limits on fixed interest rates	100%	100%	
Maturity structure fixed rate borrowing *(%)*	**Year end**	**Max**	**Min**
Under 12 months	46.0%	50%	0%
12 months to 2 years	0.1%	50%	0%
2 years to 5 years	5.0%	50%	0%
5 years to 10 years	3.5%	50%	0%
10 years to 20 years	6.9%	50%	0%
20 years to 30 years	5.7%	50%	0%
30 years to 40 years	4.5%	50%	0%
40 years to 50 years	22.2%	100%	0%
50 years to 60 years	6.1%	100%	0%
60 years to 70 years	0.0%	100%	0%
Maximum principal funds invested *>365 days*	£0.495m	£7m	Nil

4. The Main Prudential Indicators and Compliance with Limits

4.1 The Council is required by the Prudential Code to report the actual prudential indicators after the year end.

4.1.1 Capital Expenditure and its Financing

This indicator shows total capital expenditure for the year and how this was financed. The decrease in capital expenditure between revised estimate and actual as noted below in Table 3 is due to expenditure which slipped from 2019/20 into the 2020/21 capital programme, together with resources. The indicators for 2020/21 will be revised in line with this.

Table 3

	2019/20 Actual	**2019/20 Revised Estimate***
Capital expenditure:	£108.229m	£125.067m
Resourced by:		
Capital receipts and grants	£29.602m	£50.312m
Revenue	£8.397m	£7.348m
Capital expenditure - additional need to borrow	**£70.230m**	**£67.407m**

* From the mid-year Treasury Strategy – Council 30 October 2019

4.1.2 Gross Borrowing and the Capital Financing Requirement (CFR)

In order to ensure that borrowing levels are prudent, over the medium term the Council's gross borrowing must only be used for capital purposes. Gross borrowing should not therefore, except in the short term, exceed the total of the capital financing requirement in the preceding year (2019/20) plus the estimates of any additional capital financing requirement for the current (2020/21) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2019/20.

4.1.3 While the Strategic Lead - Resources reports that the Council has complied with this indicator over the medium term (as can be seen by comparing the gross debt figure at 31 March 2020 with the anticipated CFR at 31 March 2023 as detailed in Table 4 below), though in the short term the adjusted gross borrowing position exceeds the CFR as at 31 March 2020. This is due to: the Council undertaking borrowing at competitive interest rates and final capital expenditure being less than forecast once accounting adjustments have been taken into account.

Table 4

	2019/20 Actual	**2019/20 Revised Indicator***
Gross borrowing position per Table1	£509.678m	£517.851m
Long term liability	£99.942m	£100.002m
Adjusted gross borrowing position	**£609.620m**	**£617.853m**
Capital Financing Requirement	**£608.057m**	**£626.832m**

* From the mid-year Treasury Strategy – Council 30 October 2019

	2019/20 Actual
CFR at 31 March 2020	
2019/20 Actual	**£608.057m**
Estimated Movement in CFR*	
2020/21, after year end	£85.506m
2021/22	£32.497m
2022/23	£44.521m
Anticipated CFR at 31 March 2023	**£770.581m**
Gross Debt at 31 March 2020	**£609.620m**

* Estimated movement from the Treasury Strategy 2020/21 – 4 March 2020

4.1.4 The Authorised Limit

The Authorised Limit is the "Affordable Borrowing Limit" required by Section 35 of the Local Government in Scotland Act 2003. The Council does not have the power to borrow above this level. The information in Table 5 demonstrates that during 2019/20 the Council has maintained gross borrowing within its Authorised Limit.

4.1.5 The Operational Boundary

The Operational Boundary is the borrowing position that the Council expects to work around during the year, and periods where the actual position is either below or over the Boundary is acceptable subject to the Authorised Limit not being breached. The information in Table 5 demonstrates that during 2019/20 the Council has maintained gross borrowing within its Operational Boundary.

4.1.6 Actual financing costs as a proportion of net revenue stream

This indicator shows the actual impact of capital expenditure in 2019/20 compared to the projected impact of the General Services Capital Plan Refresh and the HRA Capital Plan Update as approved by Members on 4 March 2020. The cost of capital is described as loan charges within the revenue budgets

Table 5

	2019/20	
Revised Indicator - Authorised Limit*	£708.602m	
Revised Indicator - Operational Boundary*	£649.552m	
Maximum gross borrowing position during 2019/20	£612.779m	
Minimum gross borrowing position during 2019/20	£531.964m	
	Estimated	**Actual**
Financing costs as a proportion of net revenue stream:		
Non housing	4.58%	4.59%
Housing	23.48%	25.55%

* From the mid-year Treasury Strategy – Council 30 October 2019

5. Summary of the Economic Factors affecting the Strategy during 2019/20

5.1 The Economy and Interest Rates

The main issue in 2019 was to agree the way forward for the UK over the issue of Brexit and negotiations on this continue.

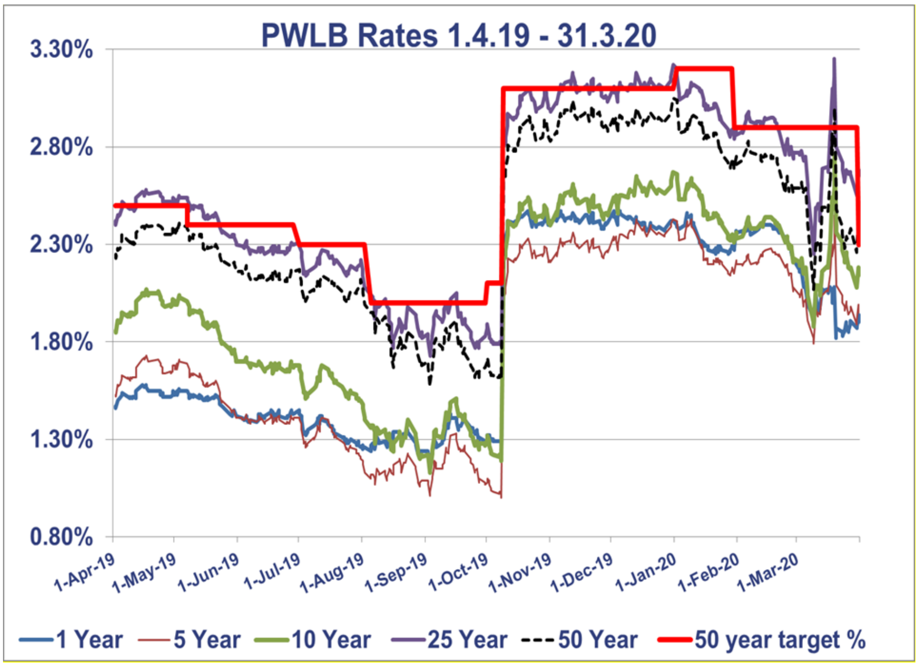
Economic growth in 2019 has been very volatile, but 2020 started optimistically. However, the three monthly GDP statistics in January were disappointing. Since then, the whole world has changed as a result of the coronavirus outbreak. What is uncertain, is the extent of the damage that will be done to businesses by the lock down period, the ongoing extent that the easing and removal of lockdown measures can continue, whether there will be a “second wave” of the outbreak, how soon a vaccine will be created (if at all) and then how quickly it can be administered to the population. This leaves huge uncertainties as to how quickly the economy will recover.

After the Monetary Policy Committee raised Bank Rate from 0.5% to 0.75% in August 2018, Brexit uncertainty caused the MPC to do nothing until March 2020. At this point it was clear that the coronavirus outbreak posed a huge threat to the economy of the UK. Two emergency cuts in Bank Rate from 0.75% occurred in March, first to 0.25% and then to 0.10%. These cuts were accompanied by an increase in quantitative easing (QE), essentially the purchases of gilts (mainly) by the Bank of England of £200bn.

5.2 Borrowing Rates in 2019/20

The graph for PWLB interest rates below shows that, although interest rates increased during October 2019, most PWLB rates have been on a general downward trend, though longer term rates did spike upwards again during March 2020.

5.3 HM Treasury imposed two changes in the margins over gilt yields for PWLB rates in 2019/20 without any prior warning - the first on 9 October 2019, which added an additional 1% margin over gilts to all PWLB rates. That increase was then partially reversed for some forms of borrowing on 11 March 2020, at the same time as the Government announced in the Budget a programme of increased spending on infrastructure expenditure. The intention is thought to be that the Treasury intends to put a stop to local authorities borrowing money from the PWLB to purchase commercial property if the aim is solely to generate an income stream (which is something than a number of Councils in England have undertaken).



6. Treasury Activity during 2019/20

6.1 **Borrowing** – The Council raised new long term loans of £50.868m and new short term loans of £218.744m during 2019/20 for the replacement of naturally maturing debt and to finance the Council's capital programme.

6.2 **Rescheduling** – No debt rescheduling has taken place in 2019/20.

6.3 **Repayment** – The Council repaid naturally maturing debt of £201.304m.

6.4 **Summary of Debt Transactions** – The overall position of the debt activity resulted in the average interest rate at 31 March year on year falling to 2.25% from 2.51%.

6.5 **Investment Policy –** The Scottish Government issued The Local Government Investments (Scotland) Regulations 2010 on 1 April 2010.

6.6 The regulations applied from 1 April 2010 and the Council's policy was first included in the annual Treasury Strategy approved by Council on 24 March 2010 with updates being included in the policy as and when required. The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

6.7 The Council's short term cash investments increased from £19.389m at the beginning of the year to £21.246m at the end of the year with an average balance of £15.934m and received an average return of 0.74% over the year. In addition to the short term cash investments the Council also had 2 long term investments in Clydebank Property Company and Hub West Scotland with a total value of £0.495m as at 31 March 2020 as identified in table 2 above (investments over 364 days).

7. Performance Indicators set for 2019/20

7.1 The treasury strategy defined a set of performance indicators covering the following areas:

7.1.1 Security - In the context of benchmarking, assessing security is a very subjective area. Security is currently evidenced by the application of minimum quality criteria to financial institutions that the Council may choose to invest in, primarily through the use of credit ratings supplied by the three main credit rating agencies (Fitch, Moody's and Standard & Poors). The Council has benchmarked security risk by assessing the historical likelihood of default for investments placed with any institution with a long term credit rating of A- (this is the minimum long term credit rating used in the Council's investment strategy). The Council's maximum security risk is that 0.09% of investments placed with financial institutions could theoretically default based on global historical data. During the year all investments within the Council's portfolio were repaid on their due dates with no defaults of the principal sums recorded.

7.1.2 Liquidity – As required by the CIPFA Treasury Management Code of Practice the Council has stated that it will "ensure that it has adequate, though not excessive, cash resources, borrowing arrangements, overdrafts or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives". In respect to liquidity as defined above the liquidity arrangements during the year were maintained in line with the facilities and benchmarks previously set by the Council as follows:

- Bank overdraft - £1.000m; and
- Liquid short term deposits of at least £5.000m available overnight.

7.1.3 Return – For the financial year the investment return averaged 0.74% which is an increase of 0.10%. Table 6 illustrates that the Council's average return identified of 0.74% was below the average return from the Council's bankers investment account (0.75%), but higher than the LIBID rates (noted in table 6) which are the local measures of return investment benchmarks approved in March 2012.

The Council's bankers (and therefore the bank with which the investment account is held) are currently the Clydesdale Bank plc which falls within the Category 3 Investment Category approved in the investment strategy approved in February 2017. Due to the credit rating of this bank this category specified a maximum limit £5million which may be held on an overnight basis only thus limiting the ability to attract interest on this account.

Table 6

Benchmark	Benchmark Return	Average Return
Internal returns above the 7 day LIBID rate	0.54%	0.74%
Internal returns above the 1 month LIBID rate	0.59%	0.74%

8. Disclosure regarding the repayment of loans fund advances for 2019/20

8.1 The policy on the prudent repayment of loans fund advances was detailed in the Mid-Year Monitoring Report 2019/20 - Treasury Management and Prudential Indicators reported to Council on 30 October 2019. The Strategic Lead - Resources can report that the policy has been complied within during 2019/20.

8.2 Table 7 shows the movement in the level of loan fund advances between 1 April 2019 and 31 March 2020.

Table 7

	Non Housing	Housing
Opening Balance at 1 April 2019	**£256.025m**	**£179.006m**
New Advances in 2019/20	£42.771m	£27.459m
Repayments in 2019/20	(£2.873m)	(£5.608m)
Adjustment for loans fund review 2019/20	£2.568m	£5.608m
Closing Balance at 31 March 2020	**£298.491m**	**£206.465m**

8.3 Table 8 details the anticipated repayment profile of the balance on the loans fund advance accounts for both non housing and housing held at 31 March 2020.

Table 8

Future Repayment Profile at 31 March 2020 (£m)	**Non Housing**	**Housing**	**Total**
Under 12 months	£3.278	£2.615	£5.894
2 years to 5 years	£11.910	£28.477	£40.387
6 years to 10 years	£17.947	£35.698	£53.645
11 years to 15 years	£25.468	£29.561	£55.029
16 years to 20 years	£22.905	£30.409	£53.314
21 years to 25 years	£15.563	£39.268	£54.832
26 years to 30 years	£11.061	£26.909	£37.970
31 years to 35 years	£7.696	£7.401	£15.098
36 years to 40 years	£8.532	£1.384	£9.916
41 years to 45 years	£10.198	£0.523	£10.721
46 years to 50 years	£11.194	£0.247	£11.441
51 years to 55 years	£14.424	£0.381	£14.805
56 years to 60 years	£20.161	£0.573	£20.734
61 year +	£118.152	£3.018	£121.170
Total	**£298.491**	**£206.465**	**£504.956**

9. Risk and Performance

9.1 The Council has complied with all relevant statutory and regulatory requirements which require the Council to identify and, where possible, quantify the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach. Ongoing consideration of future affordability and sustainability are reported and considered by Members each year when setting the Council's General Fund and HRA capital and revenue budgets.

9.2 The Council is aware of the risks of passive management of the treasury portfolio and, with the support of the Council's treasury advisers, has proactively managed its treasury position within the current economic climate taking advantage of lower interest rates where it is deemed appropriate. The Council has complied with its internal and external procedural requirements. There is little risk of volatility of costs in the current debt portfolio as the interest rates are predominantly fixed, with the majority of debt comprised of long-term loans.

9.3 Shorter-term rates and likely future movements in these rates predominantly determine the Council's investment return. These returns can therefore be volatile and, whilst the risk of loss of principal is minimised through the annual investment strategy, accurately forecasting future returns can be difficult.