Appendix 1

Mid Year Monitoring Report 2019/20
Treasury Management and Prudential Indicators: 1 April 2019 to 30 September 2019

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), which 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 have been made as yet during 2019/20).
- Statutory Instrument (SSI) 29 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.
- Statutory Instrument (SSI) 123 2016, set out statutory arrangements for local authority borrowing and lending and the requirement to maintain a loans fund and replace the statutory arrangements set out in Schedule 3 of the Local Government (Scotland) Act 1975 (Schedule 3).

1.2 The regulatory framework of treasury management requires that the Council receive a mid year treasury review, in addition to the forward looking annual treasury strategy and backward looking annual treasury report required previously. This report meets that requirement and also incorporates the needs of the Prudential Code to ensure adequate monitoring of the capital expenditure plans and the Council's prudential indicators. The treasury strategy and prudential indicators were previously reported to Council on 27 March 2019. The current position is shown (where appropriate) and revisions to the 2019/20 estimate are provided where required.

1.3 In December 2017, the Chartered Institute of Public Finance and Accountancy, (CIPFA), issued revised Prudential and Treasury Management Codes. As from 2019/20, all local authorities require to prepare a Capital Strategy which provides the following:

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services;
- an overview of how the associated risk is managed; and
- the implications for future financial sustainability

The Council's Capital Strategy was reported to and agreed by Council on 27 March 2019.

1.4 This report sets out:

- Key changes to the Council's capital activity (the prudential indicators);
- Policy on the statutory repayment of loans fund advances;
- An economic update for the first part of the 2019/20 financial year;
- The actual and proposed treasury management activity (borrowing and investment); and
- The risk approach to treasury management (the treasury management indicators).

2. Key Prudential Indicators

2.1 This part of the report is structured to update:

- The Council's capital expenditure plans and how these plans are being financed;
- The impact of the changes in the capital expenditure plans on the PIs and the underlying need to borrow;
- Compliance with the limits in place for borrowing activity; and
- Policy on the statutory repayment of loans fund advances

2.2 **Capital Expenditure** – Table A shows the current position and revised estimates for capital expenditure for 2019/20 only.

Table A:

£000	**2019/20 Original Estimate**	**Current Position**	**2019/20 Projected Outturn**
General Services	62,714	14,369	64,434
HRA	57,902	12,789	60,633
Capital Expenditure	**120,616**	**27,158**	**125,067**
Financed by:			
Capital receipts	8,487	0	8,487
Capital grants	35,854	4,564	41,825
Revenue	7,348	0	7,348
Net financing need for the year	**68,927**	**22,594**	**67,407**

2.2.1 The increase in the level of anticipated capital expenditure is mainly due to the inclusion of additional slippage following the year end and an increase in spend related to external funding. The decrease in the net financing need for the year is due to additional grants now being identified. The anticipated spends and resources are regularly reported to Members through budgetary control reports.

2.3 **Impact of changes in Capital Expenditure Plans** – Table B shows the CFR, which is the underlying external need to borrow for a capital purpose while Table C shows the expected debt position over the period.

Table B:

£000	2019/20 Original Estimate	2019/20 Projected Outturn
Opening CFR (1 April 2019)	**542,181**	**538,132**
New borrowing	57,189	55,669
LTL repayment in year	(3,102)	(3,097)
Closing CFR (31 March 2020)	**596,268**	**590,704**
Movement in CFR (from Previous year)	54,087	52,572
Net Financing need for the year (Table A)	68,927	67,407
Loan repayments in year – excluding LTL	(11,738)	(11,738)
New borrowing	**57,189**	**55,669**

Table C:

£000	2019/20 Original Estimate	Current Position	2019/20 Projected Outturn
External Debt			
Estimated/Actual Debt at 1 April 2019	438,836	441,370	441,370
Maturing Debt	(164,439)	(169,000)	(175,848)
<u>Movement in Borrowing</u>			
New Borrowing - Maturing Debt	164,439	169,000	175,848
Borrowing adjustment in relation to over borrowing at year end	0	0	(6,541)
New Borrowing – CFR (Table B)	57,189	25,000	55,669
Debt at 31 March (1)	**496,025**	**460,370**	**490,498**
Long Term Liabilities (LTL) at 1 April	103,201	103,101	103,101
LTL repayment in year (Table B)	(3,102)	(1,549)	(3,097)
LTL at 31 March (2)	**100,099**	**101,553**	**100,004**
Actual Debt at 31 March (1) + (2)	**596,124**	**561,923**	**590,502**
CFR from Table B	**596,268**	**n/a**	**590,704**
Under/(Over) Borrowing	**144**	**n/a**	**202**

2.3.1 The external debt figures included within Table C now includes both short term and long term debt. This change has been made 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. The reduction in the estimated external debt for 2019/20 is due to a reduction in the net capital financing need for the year.

2.3.2 The CFR is calculated on a year end position based on the Council's balance sheet and therefore the current position is not shown. The CFR has reduced from the original estimate due to the forecast level of capital expenditure in 2019/20 being less than budgeted. The Strategic Lead - Resources can report that the Council is on target to meet the 2019/20 revised estimates for both indicators.

2.3.3 Table C highlights that the borrowing of the Council is forecasting a minimal under-borrowed position against the CFR at 31 March 2020.

2.4 **Compliance with the limits in place for borrowing activity** – A key control over the treasury activity is a prudential indicator to ensure that over the medium term, gross borrowing will only be for a capital purpose.

Gross borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2019/20 and next two financial years. This allows some flexibility for limited early borrowing for future years.

The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent. As discussed in section 2.3, above the current position is not shown since the CFR is calculated on a year end position. The revised indicator is detailed in Table D and is illustrated by comparing the estimated gross debt as at 31 March 2020 with the CFR as at 31 March 2022. The Strategic Lead - Resources reports that no difficulties are envisaged for the current year in complying with this prudential indicator.

Table D:

£000	**2019/20 Original Estimate**	**2019/20 Projected Outturn**
CFR at 31 March 2019		
2018/19 Estimate/Actual (From Table B above)	**542,181**	**538,132**
Estimated movement in CFR		
2019/20 (From Table B above)	54,087	52,572
2020/21	49,629	49,629
2021/22	20,820	20,820
Anticipated CFR at 31 March 2022	**666,717**	**661,153**
Gross Debt at 31 March 2020 (From Table C above)	**596,124**	**590,502**

2.4.1 The Operational Boundary is detailed in Table E below and is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual debt.

Table E:

£000	**2019/20 Original Estimate**	**Current Position**	**2019/20 Projected Outturn**
External Debt	655,737	561,923	649,552

2.4.2 A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which is detailed in Table F and represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Table F:

£000	2019/20 Original Estimate	Current Position	2019/20 Projected Outturn
External Debt	715,349	561,923	708,602

2.5 **Statutory repayment of loans fund advances** – The Council is required to set out its policy for the statutory repayment of loans fund advances. The repayment of loans fund advances ensures that the Council makes a prudent provision each year to pay off an element of the accumulated loans fund advances made in previous financial years. There are no changes to the current policy previously agreed by Members.

3. Economic Outlook

3.1 The first half of 2019/20 has seen UK economic growth fall as Brexit uncertainty took a toll. In its Inflation Report of 1 August, the Bank of England was notably downbeat about the outlook for both the UK and major world economies. This mirrored investor confidence around the world which is now expecting a significant downturn or possibly even a recession in some developed economies. It was therefore no surprise that the Monetary Policy Committee (MPC) left Bank Rate unchanged at 0.75% throughout 2019, so far, and is expected to hold off on changes until there is some clarity on what is going to happen over Brexit.

As for inflation itself, CPI has been hovering around the Bank of England's target of 2% during 2019, (July 2.1%), and is likely to shift only a little upwards over the rest of 2019/20. It does not therefore pose any immediate concern to the MPC at the current time.

With regard to the labour market, despite the contraction in quarterly GDP growth of -0.2%q/q, (+1.2% y/y), in quarter 2, employment rose by 115,000 in the same quarter: this suggests that firms are preparing to expand output and suggests there could be a return to positive growth in quarter 3. Unemployment has continued near to a 44 year low, edging up from 3.8% to 3.9% on the Independent Labour Organisation measure in June; however, that was caused by a rise in the participation rate to an all-time high. Job vacancies fell for a sixth consecutive month, hitting record levels, and indicating that employers are having major difficulties filling job vacancies with suitable staff. It was therefore unsurprising that wage inflation picked up to a high point of 3.9%, (3 month average regular pay, excluding bonuses). This meant that in real terms, (i.e. wage rates higher than CPI inflation), earnings grew by about 1.8%. As the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months. This could mean that the MPC will need to take action to raise Bank Rate if there is an agreed Brexit deal as it views wage inflation in excess of 3% as increasing inflationary pressures within the UK economy.

In the political arena, if there is a general election soon, this could result in a potential loosening of monetary policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up although, conversely, a weak international backdrop could provide further support for low yielding government bonds and gilts.

3.2 The Council's treasury advisor, Link Asset Services, has provided the following interest rate forecast.

Table G:

Link Asset Services Interest Rate View	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22
Bank Rate View	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.25
3 Month LIBID	0.70	0.70	0.70	0.70	0.80	0.90	1.00	1.00	1.00	1.10	1.20
6 Month LIBID	0.80	0.80	0.80	0.80	0.90	1.00	1.10	1.10	1.20	1.30	1.40
12 Month LIBID	1.00	1.00	1.00	1.00	1.10	1.20	1.30	1.30	1.40	1.50	1.60
5yr PWLB Rate	1.20	1.30	1.50	1.60	1.70	1.70	1.80	1.90	2.00	2.00	2.10
10yr PWLB Rate	1.50	1.60	1.80	1.90	2.00	2.00	2.10	2.20	2.30	2.30	2.40
25yr PWLB Rate	2.10	2.30	2.40	2.50	2.60	2.70	2.70	2.80	2.90	3.00	3.00
50yr PWLB Rate	2.00	2.20	2.30	2.40	2.50	2.60	2.60	2.70	2.80	2.90	2.90

4. Treasury Management Activity

4.1 This part of the report is structured to update:

- The Council's expected borrowing need and details of under/(over) borrowing;
- Debt rescheduling and new borrowing;
- Debt charges; and
- Investments

4.2 **The Expected Borrowing Need** – This was set out in Table C (above) and demonstrates that at 30 September 2019 Council is currently under-borrowed to reduce risks in investments held and the cost of carry on investments (investments yield up to 0.75%, long term borrowing rates for periods greater than 25 years are currently between 1.87% to 2.03%, depending on length of term for borrowing). This introduces an element of interest rate risk, as longer term borrowing rates may rise; however, this position is being carefully monitored.

4.3 **Debt rescheduling and new borrowing** – The Council has not undertaken any debt rescheduling during the first half of 2019/20. In the year to date naturally maturing debt of £169.000m has been repaid which has been mainly funded by loans from other local authorities.

4.4 **Debt Charges** – The revised estimate for debt charges for both the General Fund and the HRA is shown in Table H.

Table H:

£000	2019/20 Original Estimate	Current Position	2019/20 Revised Estimate
Borrowing	22,637	11,195	22,390
Other Long Term Liabilities	10,500	5,156	10,311
Total	**33,137**	**16,351**	**32,701**

4.5 **Investments** – The objectives of the Council's investment strategy are to ensure the re-payment of the principal and interest of its investments on time with the level of investment return being a secondary objective. Following on from the economic background above, the current investment climate has one over-riding risk consideration which is the risk of default.

4.5.1 The Council held £20.844m of cash investments at 30 September 2019, and the constituent parts of the investment position are detailed in Table I:

Table I:

£000	Country	< 1 Year	1 – 2 Years	2 – 3 Years
Banks	UK	1,844	Nil	Nil
Money Market Fund		13,000	Nil	Nil
Local Authorities		6,000	Nil	Nil
Total		20,844	Nil	Nil

4.5.2 Table J details the revised budget position for investment income. The original estimate has decreased by £0.005m.

Table J:

£000	2019/20 Original Estimate	Current Position	2019/20 Revised Estimate
Investment Income	118	57	113

4.5.3 A regulatory development to address risk is the consideration and approval of benchmarks relating to investment security, liquidity and the level of return. Benchmarks are currently widely used to assess the level of return and investment performance, however the application of security and liquidity benchmarks are more subjective in nature.

- **Security** - The Council's maximum security risk benchmark for the current portfolio in relation to investment periods of up to one year (when compared to historic default tables) was set at 0.09% and the Strategic Lead - Resources can report that there have been no defaults of principal sums invested in the year to date.

- **Liquidity** – The Strategic Lead - Resources can report that liquidity arrangements were adequate during the year to date and that the liquidity facilities and benchmarks set by the Council as noted below were maintained:

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

- **Return on Investments** – The Strategic Lead - Resources can report that investment return to date average 0.75%. Table K illustrates how this average return compares with the local benchmarks.

Table K:

Benchmark	Benchmark Return	Average Return
7 day LIBID rate	0.57%	0.75%
1 month LIBID rate	0.60%	0.75%
Council's Instant Access Account	0.75%	0.75%

5 Key Treasury Management Indicators

5.1 This part of the report is structured to update:

- Actual and estimates of the ratio of financing costs to net revenue stream;
- Upper limits on interest rate exposure:
- The maturity structure of borrowing; and
- Total principal sums invested.

5.2 **Actual and estimates of the ratio of financing costs to net revenue stream** – This indicator (as shown below in Table L) identifies the trend in the cost of capital (financing costs net of interest and investment income) against the net revenue stream.

Table L:

	2019/20 Original Estimate	2019/20 Revised Estimate
General Fund	10.55%	9.70%
HRA	27.72%	27.31%

5.3 **Upper Limits On Fixed and Variable Rate Exposure** – These indicators identify a maximum limit for fixed and variable interest rates based upon the debt position and were set at 100% and 50% respectively for 2019/20. The Strategic Lead – Resources reports that the Council operates within these limits.

5.4 **Maturity Structures Of Borrowing** – These maximum limits are set to reduce the Council's exposure to large fixed rate loans (those instruments which carry a fixed interest rate for the duration of the instrument) which are due to naturally mature in any given period as detailed in Table M and show that the Council operates within limits set.

Table M:

Maturity Structure of Fixed Interest Rate Borrowing	2019/20 Original Limits	Current Position
Under 12 months	50%	29.28%
12 months to 2 years	50%	12.61%
2 years to 5 years	50%	2.54%
5 years to 10 years	50%	4.48%
10 years to 20 years	50%	7.78%
20 years to 30 years	50%	6.41%
30 years to 40 years	50%	7.21%
40 years to 50 years	100%	17.35%
50 years to 60 years	100%	12.35%
60 years to 70 years	100%	0%

5.5 **Total Principal Funds Invested** – These limits are set to reduce the need to temporarily borrow to cover any unexpected expenditure, and show limits to be placed on investments with final maturities beyond each year-end. The Council currently invests sums for periods greater than 365 days in Clydebank Property Company and hub West Scotland as detailed in Table N.

Table N:

	2019/20 Original Estimate	Current Position	2019/20 Revised Estimate
Principal sums invested > 365 days (maximum limit £7m)	£0.547m	£0.547m	£0.547m