

## TREASURY MANAGEMENT INTERIM REPORT - 2019/20

<b>Head of Service/Contact:</b>	Lee Duffy, Chief Finance Officer
<b>Urgent Decision?(yes/no)</b>	No
<b>If yes, reason urgent decision required:</b>	N/A
<b>Annexes/Appendices (attached):</b>	None
<b>Other available papers (not attached):</b>	Treasury Management Strategy 2019/20 CIPFA Prudential Code Code of Practice for Treasury Management in Local Authorities (CIPFA)

### Report summary

This report sets out an update on treasury management performance for the first six months of 2019/20.

### Recommendation (s)

That the Panel:

- (1) **Receives the presentation from Link Asset Services – Treasury Solutions;**
- (2) **Notes the performance on return of investments for the first six months of 2019/20;**
- (3) **Notes the current investment decisions being made within the terms sets out in the Treasury Management Strategy.**

### 1 Implications for the Council's Key Priorities, Service Plans and Sustainable Community Strategy

- 1.1 The Council's Treasury Management Strategy supports the achievement of the Council's Medium Term Financial Strategy.
- 1.2 The Treasury Management Strategy for 2019/20 agreed by Council in February aims to ensure maximum return on investments for the Council within reasonable risk constraints.

# Financial Policy Panel

## 3 December 2019

### **2 Background**

- 2.1 The Council's Treasury Management Policy accords with the Chartered Institute of Public Finance and Accountancy's (CIPFA's) Code of Practice on Treasury Management in the Public Services.
- 2.2 The policy requires officers to produce an interim report on investment performance to a meeting of the Financial Policy Panel. This report covers the performance of the treasury management function for the period 01 April 2019 to 30 September 2019.
- 2.3 The CIPFA Code also requires that adequate training be provided to members with responsibility for treasury management. To meet this requirement, an officer from Link Asset Services – Treasury Solutions will attend the meeting to provide a presentation to members on current treasury management issues.

### **3 Overview of Treasury Management**

- 3.1 The treasury function deals with the management of cash funds held by the Council. The level of funds held during the year will vary but, on average, currently amounts to around £19 million at September 2019 (£15m at September 2018, £30m at September 2017).
- 3.2 The current average balance is significantly lower than 2017 levels, because the Council deployed £20.1m of its cash balances to reduce the borrowing requirement associated with commercial property investments since 2017. By deploying cash balances in this way, the Council has minimised its borrowing with the Public Works Loan Board, which typically attracts interest payable at circa 3.0% in the current environment.
- 3.3 The aim of treasury management is to ensure that funds are invested with institutions that balance the need to maximise investment returns with that of minimising risk on the monies invested. This means not investing in banks/building societies that are offering high investment returns but are at high risk of defaulting (for example the Icelandic Banks in 2008).
- 3.4 Before an investment decision is made, officers will investigate any proposed counterparty to ensure its financial rating makes it eligible for investment. Even if the institution meets the criteria as set out in the financial strategy, independent advice will be sought from our external financial advisors before the investment is made.

### **4 Security, Liquidity and Yield**

- 4.1 The Council's investment strategy and practice is to put security of investment at a higher priority than rate of return/yield. The day to day practice continues to be reviewed and refined, within the boundaries of the approved policy, in response to challenging market conditions. The cornerstones of current policy/practice are:

## Financial Policy Panel

### 3 December 2019

- 4.1.1 to restrict lending to only those institutions which fit the Council's policy in terms of financial standing, credit ratings etc;
- 4.1.2 generally, to restrict lending to the short-term (typically 3 to 6 months or less) or to cover precept dates for the remainder of the year;
- 4.1.3 to update financial limits to each institution depending the quality of their financial ratings.

## 5 Current Performance

- 5.1 The average return from investments for 2019/20 was budgeted at 0.8%. This amounted to total budgeted income for the year of £96,000, generated on reserves, working balances and cash flow.
- 5.2 The performance for the first six months of 2019/20 on the Council's investments were as follows;

	Average Investment (Apr-Sept) £'m	Interest Received (Apr-Sept) £'000	Average Rate of Return %
<b>Internally Managed Funds</b>			
Money Market Funds	7.0	30.9	0.88
Fixed Rate Deposits	3.7	20.8	1.14
Interest Bearing Account	0.8	0.6	0.14
<b>Total Internally Managed</b>	<b>11.5</b>	<b>52.3</b>	<b>0.91</b>
<b>Externally Managed Funds</b>			
Aberdeen Asset Management	7.5	33.0	0.88
<b>Grand Total</b>	<b>19.0</b>	<b>85.3</b>	<b>0.90</b>

- 5.3 To date, £85,300 interest has been earned as at the end of September, which significantly exceeds the profiled budgeted income of £48,000 for the same period. Officers anticipate that this positive performance can be maintained over the second half of the year, as the Bank of England base rate has remained steady at 0.75% across the year to date.
- 5.4 The average return achieved for the first six months of 2019/20 of 0.90% compares favourably with the benchmark average seven day London Interbank Bid (LIBID) rate of 0.57%.

# Financial Policy Panel

## 3 December 2019

- 5.5 The Council has achieved this performance by following the strategy of investing the majority of its long to medium term funds with its external fund manager, Aberdeen Asset Management and investing in a one year fixed rate investment with a return of one percent. Short term funds have been invested in money market funds or in an interest bearing instant access account.

### **6 Internally Managed Funds**

#### **Money Market Funds**

- 6.1 Money market funds are pooled investments that allow instant access to these monies. The benefit of MMFs is that the risk on the investment is very low as the money invested in the fund is spread across a range of counterparties, which limits the exposure of a significant sum being invested with a defaulting counterparty.
- 6.2 The return made on money market funds of 0.88% is higher than the benchmark of 0.57%. Investment in money market funds has been limited to short term investments from surplus funds which will need to be called back with no notice required.

#### **Fixed Rate Term Deposits**

- 6.3 As at the end of September the Council had one fixed term deposit of £5,000,000, invested at a rate of 1.3% with a maturity date of July 2020.
- 6.4 The current strategy and recent guidance obtained from our independent financial advisors is to limit fixed term investments to a period of one year until there is improved stability within the financial markets.

#### **Interest Bearing Accounts**

- 6.5 Interest bearing accounts offer the same instant access as the money market funds and deliver a rate of return linked to base rate set by the Bank of England.
- 6.6 Rates achievable on this account have been cut significantly in recent years and it is now only used if other investments have reached their counterparty limits. The risk on these investments is higher than the money market funds as money is deposited with one counterparty. Funds invested in this type of investment tend to be surpluses of daily cash flows which need to be called back at short notice.
- 6.7 The return made on interest bearing accounts of 0.14% compared unfavourably to the benchmark of 0.57%. As such, the interest bearing account was utilised less frequently, typically when limits with other counter parties were reached.

# Financial Policy Panel

## 3 December 2019

### **7 Externally Managed Funds**

- 7.1 Aberdeen Asset Management plc, previously Scottish Widows, has been the Council's external fund manager since October 2007.
- 7.2 Initially, the external fund manager produced some exceptional returns for the Council. Since October 2009 returns have fallen back as opportunities to deliver significant returns have become very limited due to difficult market conditions. However, the fund manager has still consistently produced returns above the benchmark.
- 7.3 The fund manager has advised an anticipated overall return on the fund of around 1.0% by the end of the year.
- 7.4 The Council has adopted a policy of investing the majority of our medium to long term funds with this fund manager. This has two benefits to the Council: the first is it minimises the Council's risk, as the funds invested with Aberdeen Asset Management plc are spread across a wide portfolio of financial institutions. This results in the overall exposure to a potential defaulting bank being limited to a small percentage of the overall holding; the second benefit is that Aberdeen Asset Management plc are able to attract more favourable rates due to the size of the fund and having access to detailed information regarding the various institutions.
- 7.5 Due to the performance of Aberdeen Asset Management plc over the past eleven years, officers intend to continue to use Aberdeen Asset Management plc as the external fund manager and review the position again in 12 months.

### **8 Treasury Management Policy**

- 8.1 In previous years the Council has recognised the increased levels of risk due to the uncertainty in the financial markets and consequently restricted the number of investments held over a fixed term.
- 8.2 Officers have entered into a fixed rate one year investment and are in the process of exploring other types of investments that potentially can increase yields without significantly increasing the risk to the capital invested.
- 8.3 Should a commercial property acquisition, funded through borrowing, materialise during the current year, officers will explore the option of using cash balances to reduce the external borrowing requirement. External borrowing typically attracts interest payable at circa 3.0% in the current environment.

# Financial Policy Panel

## 3 December 2019

- 8.4 The Council continues to use Money Market Funds for internal investments as they minimise exposure to counterparty risk. Current returns on these funds are slightly higher than those offered from interest bearing accounts, and these funds also allow for maximising investment of short term cash surpluses during the year and also improve the efficiency of cash flow management.

### 9 Interest Equalisation Reserve

- 9.1 The interest equalisation reserve was established several years ago to enable variations in investment returns to be accommodated within the general fund budget without having an adverse effect on the levels of funds available for the delivery of services in year.
- 9.2 With base rates and investment returns remaining at relatively low levels, and with the Council's cash balances lower than prior years, the funds in this reserve may be needed to achieve budgeted general fund income in the coming years.
- 9.3 As agreed at Financial Policy Panel in September 2019, the balance on this reserve has been reduced from £631,000 to £400,000 at 30 September, with £231,000 transferred to the Property Income Equalisation Reserve to assist the Council in balancing its revenue budget over the four-year period of the next Medium Term Financial Strategy.
- 9.4 The level of this reserve will be re-assessed in the 2020/21 budget report in February 2020.

### 10 Financial and Manpower Implications

- 10.1 The Council's budget anticipates the equivalent of £96,000 of interest to help fund services in 2019/20 calculated as follows:

	<b>Budgeted £</b>	<b>Forecast £</b>
Interest earned in year	96,000	172,000
Less Interest credited to specific provisions	(58,000)	(58,000)
<b>Interest used to fund General Fund services</b>	<b>38,000</b>	<b>114,000</b>

- 10.2 The forecast interest at the end of 2019/20 is anticipated to outperform the budget, generating a surplus of £76,000 above the budgeted income. It is therefore anticipated that a contribution to the interest equalisation reserve can be made to fund services in future years.
- 10.3 **Chief Finance Officer's comments:** *Financial implications are set-out in the body of the report.*

# Financial Policy Panel

## 3 December 2019

### **11 Legal Implications (including implications for matters relating to equality)**

11.1 There are no particular equalities or other legal implications for the purpose of this report.

### **12 Sustainability Policy and Community Safety Implications**

12.1 None for the purposes of this report.

### **13 Partnerships**

13.1 There is partnership working with the external fund manager and the treasury consultants, but no particular implications arise from this report.

### **14 Risk Assessment**

14.1 Investments with our external fund manager are considered low risk as the money invested in the fund is spread across a range of counterparties, this limits the exposure of a significant sum being invested with a defaulting counterparty. The total value of the fund is currently £4.8bn.

14.2 The Treasury Management Strategy sets out that investment decisions must be based first and foremost on security, then liquidity and finally yield, in order to minimise risk.

### **15 Conclusion and Recommendations**

15.1 Both internal and external investments for the first six months of 2019/20 have exceeded the benchmark of 7 day LIBID rate.

15.2 It is recommended that the Panel:

15.2.1 Receives the presentation from Link Asset Services – Treasury Solutions;

15.2.2 Notes the performance on return of investments for the first six months of 2019/20;

15.2.3 Notes the current investment decisions being made within the terms sets out in the Treasury Management Strategy.

**Ward(s) affected:** (All Wards);