Report to	Cabinet	**Item**
Report of	Chief finance officer	12
Subject	Treasury Management Full Year Review Report 2017-18	

Purpose

This report sets out the Treasury Management performance for the year to 31 March 2018.

Recommendation

To recommend that council note the report and the treasury activity for the year to 31 March 2018.

Financial implications

The report has no direct financial consequences however it does report on the performance of the council in managing its borrowing and investment resources.

Ward/s: All wards

Cabinet member: Councillor Kendrick, resources

Contact officers

Karen Watling, chief finance officer 01603 212440

Background documents

None

Report

Background

1. The council is required by regulations issued under the Local Government Act 2003 to produce an annual review of its treasury management activities and the actual prudential and treasury indicators for 2017-18. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

2. This report details the results of the council's treasury management activities for the financial year 2017-18. It compares this activity to the Treasury Management Strategy for 2017-18, approved by Full Council on 21 February 2017. It will also detail any issues that have arisen in treasury management during this period.

Introduction

3. Treasury Management relates to the policies, strategies and processes associated with managing the cash and debt of the council through appropriate borrowing and lending activity. It includes the effective control of the risks associated with the lending and borrowing activity and the pursuit of optimum performance consistent with the risks.

4. For the 2017/18 financial year the minimum reporting requirements were that full council should receive the following reports:
    - an annual Treasury Management Strategy in advance of the year (council 21 February 2017).
    - a mid-year Treasury Management Review report (Cabinet 17 January 2017).
    - an annual review following the end of the year describing the activity compared to the strategy (this report).

5. The regulatory environment places responsibility on members to review and scrutinise 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 which have previously been approved by members. This report summarises the following:-
    - Capital activity during the year (paragraphs 6 & 7)
    - Impact of this activity on the council’s underlying indebtedness (the Capital Financing Requirement) (paragraphs 8-14)
    - The actual prudential and treasury indicators (paragraphs 15-19)
    - Overall treasury position identifying how the council has borrowed in relation to this indebtedness, and the impact on investment balances (paragraphs 20-25)
    - Review of treasury strategy (paragraphs 26-28)
    - Borrowing strategy and detailed debt activity (paragraphs 29-31)
    - Investment strategy and detailed investment activity (paragraphs 32-39)

The council’s Capital Expenditure and Financing 2017-18

6. The capital programme was revised during 2017-18 from that agreed by full council at its meeting on 21 February 2017. The revised capital programme shown in the table below was reported in the out-turn report to Cabinet on 13 June 2018. Actual capital spending was under budget for the year by £55.870m. This capital spending includes both capitalised additions and capital loans made in year. Consequently the actual level of revenue and borrowing needed to finance the expenditure was less than that estimated. The actual capital expenditure forms one of the required prudential indicators. The table below shows the estimates and then the actual capital expenditure for 2017-18 and how this was financed in the year:

Table 1

Capital Expenditure	**2017/18 Original Estimate £m**	**2017/18 Revised Estimate (30.09.17) £m**	**2017/18 Actual £m**	**(Underspend) /Overspend £m**
Non-Housing Capital expenditure	35,075	67,489	19,221	(48,268)
Non-Housing Capital Loans	12,593	12,593	10,856	(1,737)
HRA Capital expenditure	51,281	47,094	28,636	(18,458)
	86,356	114,583	58,713	(55,870)
Financed by				
Capital Receipts	16,246	12,382	7,284	(5,098)
Capital Grants	8,897	10,713	6,309	(4,404)
Capital Reserves	6,925	-	-	-
Revenue	22,366	19,927	13,273	(6,654)
Major Repairs Reserve	-	13,871	7,001	(6,870)
	54,434	56,893	33,867	(23,026)
Borrowing need for the Year	**31,922**	**57,690**	**24,842**	**(32,848)**

7. Capital expenditure may either be:
   - Financed immediately through the application of capital or revenue resources e.g. capital receipts, capital grants, revenue contributions etc.), which has no impact on the council's borrowing need; or
   - If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need, which will be satisfied by either external or internal borrowing.

Council's overall borrowing need

8. The council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). The CFR arises as the council incurs capital spending and then if it does not apply resources immediately to finance the capital spend, i.e. capital receipts, capital grants, capital reserves or revenue, a borrowing need arises. The 2017-18 CFR year-end balance is the cumulative total of the 2017-18 unfinanced capital expenditure i.e. £24.842m, and prior years' unfinanced capital.

9. Treasury Management includes addressing the funding requirements for this borrowing need; it also includes maintaining a cash position to ensure sufficient cash is available to meet the capital expenditure and cash flow requirements. This may be sourced through borrowing from external bodies, e.g. the Government

through the Public Works Loan Board (PWLB) or the money markets, or utilising temporary cash resources within the council (known as internal borrowing).

10. Reducing the CFR – the council's (non-HRA) underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. This requirement is met by making an annual revenue charge, called the Minimum Revenue Provision (MRP), to reduce the CFR. This is effectively a repayment of the non-HRA borrowing need (there is no statutory requirement to reduce the HRA CFR).

11. The total CFR can also be reduced by either:

    - the application of additional capital financing resources (such as unapplied capital receipts)
    - charging more than the statutory MRP each year through a Voluntary Revenue Provision (VRP).

12. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External borrowing can be taken or repaid at any time, but this does not change the CFR.

13. The council's CFR for the year is shown below, and is a key prudential indicator. It includes leasing schemes on the balance sheet, which increase the council's borrowing need. No borrowing is actually required against these schemes as a borrowing facility is included in the contract.

Table 2

	2017/18 Original Estimate	2017/18 Revised Estimate	2017/18 Actual
General Fund	**£m**	**£m**	**£m**
Opening balance	32.739	32.081	34.673
Add: Unfinanced capital expenditure*	31.922	57.690	24.597
Less: MRP	(0.302)	(0.344)	(0.352)
General Fund closing balance	64.359	89.427	58.918
HRA	**£m**	**£m**	**£m**
Opening balance	211.634	205.717	205.717
Add: Unfinanced capital expenditure	-	-	-
HRA closing balance	217.665	205.717	205.717
Total Capital Financing Requirement	**282.024**	**295.144**	**264.635**

* The actual unfinanced capital expenditure differs from Table 1 by £0.245m as a result of loan repayments received in year which have reduced the capital financing requirement.

14. Borrowing activity is constrained by prudential indicators for borrowing and the CFR, and by the authorised limit.

The actual prudential and treasury indicators

15. **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 council 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 (2016/17) plus the estimates of any additional capital financing requirement for the current (2017/18) and next two financial years. This essentially means that the council is not borrowing to support revenue expenditure. This indicator allows the council some flexibility to borrow in advance of its immediate capital needs. The table below highlights the council's gross borrowing position against the CFR. The council has complied with this prudential indicator.

Table 3

	2017/18 Original Estimate £m	**2017/18 Revised Estimate £m**	**2017/18 Actual £m**
Gross borrowing	255.283	291.576	201.392
CFR	282.203	295.051	264.635
Over Borrowed/(Under Borrowed)	**(26.920)**	**(3.475)**	**(63.243)**

16. **The authorised limit** - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. The council does not have the power to borrow above this level. The table below demonstrates that during 2017/18 the council has maintained gross borrowing within its authorised limit.

Table 4

	2017/18 Original Estimate £m	**2017/18 Revised Estimate £m**	**2017/18 Actual £m**
Authorised Limit for external debt			
Borrowing	253.707	290.000	290.000
Other long term liabilities	1.576	1.576	1.576
Total Agreed Authorised Limit	**255.283**	**291.576**	**291.576**
Operational boundary for external debt			
Borrowing	253.107	270.000	270.000
Other long term liabilities	1.576	1.576	1.576
Total Agreed Operational Boundary	**254.683**	**271.576**	**271.576**
External debt (including other long term liabilities e.g. finance leases)	**215.856**	**266.085**	**202.729**

17. **The operational boundary** – the operational boundary is the expected borrowing position of the council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

Actual financing costs as a proportion of net revenue stream

18. This indicator shows what the cost of capital is (borrowing and other long term obligation costs net of investment income) as a percentage of the net revenue stream (the amount that is funded by government grants and council tax payers) for the general fund and the rental income (paid by tenants) for the HRA.

19. There is a notable difference when comparing the actual affordability percentages and estimated affordability percentages for both the general fund and the HRA. This is due to a review of the method of calculation. The calculation of the actual percentage follows the method given in the CIPFA guidance whereas the estimate used a different basis. Using the prescribed method in the guidance will ensure consistency year on year and will also allow comparison with other authorities on a consistent basis (if the council wanted to compare like with like). For comparison purposes the revised methodology has been applied to the 17/18 budget figures to provide comparable percentages for the 17/18 actual outturn.

Table 5

Affordability of financing costs	2017/18 Strategy Estimate	2017/18 Strategy Reworked	2017/18 Actual
General fund - financing costs as a percentage of net revenue stream	7.64%	2.15%	2.56%
HRA - financing costs as a percentage of rental income	10.25%	37.68%	40.33%

Treasury Position as at 31 March 2018

20. The council's debt and investment position is managed by the in-house treasury management team. All activities are undertaken primarily to ensure security for investments, to ensure that there is adequate liquidity for revenue and capital activities, and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity detailed in the council's Treasury Management Practices.

21. The council's actual borrowing position at 31 March 2018 and activity during 2017-18 is detailed in the table below:

Table 6

Borrowing activity 2017-18 (excluding finance leases)	PWLB loans £m	Market loans £m	Total £m	Average interest rate %
Opening balance (1 April 2017)	203.107	5.000	208.107	4.45%
New borrowing taken	-	-	-	
Borrowing matured/repaid	(7.000)	-	(7.000)	
Closing balance (31 March 2018)	**196.107**	**5.000**	**201.107**	**3.88%**
Authorised limit for external debt			291.576	

22. The maturity structure of the debt portfolio was as follows:

Table 7

Maturity Structure of fixed rate borrowing	Upper Limit per Strategy %	%	31-Mar-18 £m
Under 12 months	10	1	2.000

Between 12 months and 2 years	10	0	0.000
Between 2 years and 5 years	30	7	53.459
Between 5 years and 10 years	50	60	119.700
Over 10 years	95	13	25.948
Total borrowing			**201.107**

23. The upper limit set in the strategy for maturity between 5-10 years has been exceeded at the end of 2017/18. This is the result of a scheduled repayment of Housing Revenue Account self-financing debt moving into the lower maturity category at the end of the year, combined with the deferral of planned long term borrowing because cash balances have been sufficient in the year. The strategy limits will be reviewed as part of the wider consideration of the council's future borrowing requirements.

24. The following table shows the movement in investments in the year. The decrease in year was due to investments being liquidated to fund commercial property investments and the loan to Norwich Regeneration Ltd.

Table 8

Investments	**Actual 31 March 2017**	**Net movements in year**	**Actual 31 March 2018**
	£m	**£m**	**£m**
Short term			-
Banks	28.000	(20.000)	8.000
Building Societies	27.400	(15.400)	12.000
Local Authorities	-	3.000	3.000
Cash Equivalents			
Banks	10.660	(3.890)	6.770
Building Societies	-	1.650	1.650
Local Authorities	7.500	(3.250)	4.250
Money Market Funds	-	15.000	15.000
Total Internally Managed Funds	**73.560**	**(22.890)**	**50.670**

25. The maturity structure of the investment portfolio was as follows:

Table 9

	31 March 2017	**31 March 2018**
	£m	**£m**
Under 1 year	73.560	50.670
	73.560	**50.670**

Borrowing Strategy for 2017-18

26. The council maintained an under-borrowed position in 2017/18. This means that the capital borrowing need (the CFR) has not been fully funded with loan debt as cash supporting the council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is relatively high.

27. Going forwards caution will be adopted with the 2018-19 treasury operations. The Chief finance officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

    - if it was felt that there was a significant risk of a sharp fall in long and short term rates (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
    - if it was felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.

28. The Chief Finance Officer (CFO) advise that it is very likely that the council will need to undertake fixed rate long term borrowing within the next few months. Any decisions will be reported to Cabinet at the next available opportunity.

Policy on borrowing in advance of need

29. The council's policy is not to borrow more than, or in advance of, its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the council can ensure the security of such funds. The policy has been complied with in 2017/18.

Borrowing Outturn for 2017-18

30. No borrowing was undertaken during the year because cash balances have been sufficient in the short term to cover the 2017/18 unfinanced capital and short term investments. During 2017-18 £7.000m of PWLB debt was repaid.

31. During 2017-18 the council paid £8.4m in interest costs on external loans, this compares to a budget of £8.5m.

Investment Strategy for 2017-18

32. The council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Capita Asset Services (formerly Sector)al Guidance Notes ("the CIPFA TM Code"). The council's investment priorities will be security first, liquidity second, then return.

33. In accordance with the above guidance from the Government and CIPFA, and in order to minimise the risk to investments, the council applies minimum acceptable credit criteria in order to generate a list of highly creditworthy counterparties which also enables diversification and thus avoidance of concentration risk.

34. The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk.

Investment Outturn for 2017-18

35. The investment activity during the year conformed to the approved strategy, and the council had no liquidity difficulties.

Reserves

36. The council's cash balances comprise revenue and capital resources and cash flow monies. The council's reserves comprised:

Table 10

Balance Sheet Reserves	**31-Mar-17**	**31-Mar-18**
	£m	**£m**
General Reserves	44.728	43.644
Earmarked Reserves	3.701	8.360
Useable Capital receipts	26.554	33.997
Capital grants Unapplied	4.879	8.079
Major Repairs Reserve	-	7.000
Total	**79.862**	**101.080**

Investments held by the Council

37. The council's year-end balance of cash and short term investments was £50.670m. These internally managed funds earned an average rate of return of 0.61%. The target performance indicator was the average 7-day LIBID rate + 0.4% for the year, which was 0.62%.

38. The council is part of a benchmarking group (run by our treasury management advisors, Link Asset Services) across Norfolk, Suffolk & Cambridgeshire. The table below shows the performance of the council's investments when compared with this benchmark group, and also when compared with the non-metropolitan districts and all authorities that use Link's benchmarking group facility.

Table 11

Link benchmarking - position at 31 March 18				
	Norwich	**Benchmark Group (7 of 12)**	**Non met districts (90)**	**All authorities (223)**
WARoR[1]	0.61%	0.65%	0.69%	0.66%
WA Risk[2]	3.40	3.97	3.36	3.19
WAM[3]	48	111	99	92
WATT[4]	92	188	194	178

1. **WARoR** – Weighted average rate of return. This is the average annualised rate of return weighted by the principle amount in each rate
2. **WA Risk** – Weighted average risk number. Each institution is assigned a colour to a suggested duration using Sector's credit methodology. The institution is assigned a number based on its colour and an average, weighted using principal amount, of these numbers is calculated. A number of 5.13 means between 0 to 3 months
3. **WAM** - Weighted average time to maturity. This is the average time, in days, until the portfolio matures, weighted by the principle amount
4. **WATT** – Weighted average total time. This is the average time, in days, that deposits are lent out for, weighted by the principle amount

The number in brackets in the headings is the number of authorities that provided information to Link

39. The council's average investments return (0.61%) is lower than that for the benchmark group (0.65%), and it was also lower than both the 90 non-met authorities at 0.69% and the population of 223 local authorities at 0.66%. The slightly lower average investment return when compared with other similar

authorities reflects the council's policy of keeping funds readily available so that if an opportunity to acquire an investment property arose the funds would be available to purchase it at short notice.

Integrated impact assessment	NORWICH City Council

The IIA should assess **the impact of the recommendation** being made by the report
Detailed guidance to help with completing the assessment can be found here. Delete this row after completion

Report author to complete	
Committee:	Cabinet
Committee date:	12 September 2018
Head of service:	Karen Watling
Report subject:	Full Year Treasury Management Report
Date assessed:	31 August 2018
Description:	This report is to inform members of the actual treasury activity for the year and compares that to the treasury management indicators set in the Treasury Management Strategy for 2017-18.

	Impact			
Economic (please add an 'x' as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Finance (value for money)	☐	☒	☐	The report has no direct financial consequences however it does report on the performance of the Council in managing its borrowing and investment resources
Other departments and services e.g. office facilities, customer contact	☒	☐	☐	
ICT services	☒	☐	☐	
Economic development	☒	☐	☐	
Financial inclusion	☒	☐	☐	
Social (please add an 'x' as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Safeguarding children and adults	☒	☐	☐	
S17 crime and disorder act 1998	☒	☐	☐	
Human Rights Act 1998	☒	☐	☐	
Health and well being	☒	☐	☐	

	Impact			
Equality and diversity (please add an ‘x’ as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Relations between groups (cohesion)	☒	☐	☐	
Eliminating discrimination & harassment	☒	☐	☐	
Advancing equality of opportunity	☒	☐	☐	
Environmental (please add an ‘x’ as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Transportation	☒	☐	☐	
Natural and built environment	☒	☐	☐	
Waste minimisation & resource use	☒	☐	☐	
Pollution	☒	☐	☐	
Sustainable procurement	☒	☐	☐	
Energy and climate change	☒	☐	☐	
(Please add an ‘x’ as appropriate)	**Neutral**	**Positive**	**Negative**	**Comments**
Risk management	☒	☐	☐	

Recommendations from impact assessment
Positive
Negative
Neutral
Issues