

Treasury Management Strategy Statement and Annual Investment Strategy Update 2019/20

The Treasury Management Strategy Statement (TMSS) for 2019/20 was approved by Council on 27th February 2019.

At a meeting of the Cabinet on 29th October 2019 a proposed Protocol was agreed in relation to the South Holland Community Reserve of £500k which will be used to provide loans to Parish Councils for capital works and/or projects.

These loans will be available for up to 15 years at a rate of 1% above the Bank of England Base Rate (currently 0.75%).

It is proposed to amend the Treasury Management Strategy Statement to add Parish Councils in the table of "Non-Specified Investments with Maturities in Excess of 1 Year". This addition will read as follows:

Category	Minimum Credit Criteria	Use	Max % of non-specified investments	Maximum maturity period
Parish Councils (SHDC Community Reserve)	N/A	In-house	10%	15 Year

The Council's Capital Position (Prudential Indicators)

This part of the report is structured to update:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

Prudential Indicator for Capital Expenditure

The following table shows the revised estimates and financing of capital expenditure and the changes since the capital programme was agreed at the Budget. It also highlights the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure.

Capital Expenditure	2019-20 Original Programme £'000	2019-20 Latest Approved £'000	Actual As At 30-09-19 £'000	2019-20 Forecast Outturn £'000
Housing Revenue Account (HRA)	12,532	10,207	3,123	9,908
General Fund	1,530	6,850	770	6,782
Commercial activities/non-financial investments *	4,484	5,405	1,320	4,161
Total spend	18,546	22,462	5,213	20,851
Financed by:				
Capital receipts	728	793	238	793
Capital grants and Contributions	1,880	2,203	833	2,203
Major Repairs Reserve	7,552	4,878	2,545	4,878
Direct Revenue Funding	5,549	9,146	515	8,779
Total financing	15,709	17,020	4,131	16,653
Borrowing need	2,837	5,442	1,082	4,198

*Commercial activities/non-financial investments relate to areas such as capital expenditure on investment properties, loans to third parties etc.

The General Fund capital expenditure programme has increased from an original budget of £6.014m to £12.255m. The key items that have resulted in this increase are as follows:

- Capital Acquisitions for Growth and Commercialisations £895k
- Operational Acquisitions £2.5m
- Food Enterprise Zone £800k
- Housing Infrastructure Funding £1m

The borrowing need shown in the above table is the Council's purchase of an additional equity stake in Welland Homes and the loans made to Welland Homes. This capital expenditure has not been financed and therefore creates a borrowing requirement. Rather than take out external borrowing, the Council is utilising its cash balances and internally borrowing to finance the capital expenditure.

Changes to the Prudential Indicators for the Capital Financing Requirement (CFR), External Debt and the Operational Boundary.

The following table shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period. This is termed the Operational Boundary.

	2019-20 Original Estimate For Year End £'000	2019-20 Latest Approved For Year End £'000	Position As At 30-09-19 £'000	2019-20 Forecast Outturn For Year End £'000
Prudential Indicator – CFR				
CFR – housing	68,439	68,439	68,439	68,439
CFR – non housing	1,440	1,440	1,440	1,440
Commercial activities/ non-financial investments	6,952	12,394	8,034	11,150
Total CFR	76,831	82,273	77,913	81,029
Net movement in CFR	2,837	5,442	1,082	4,198
Prudential Indicator – External Debt / Operational Boundary				
Borrowing	67,456	67,456	67,456	67,456
Other long term liabilities	0	0	0	0
Total debt 31 March	67,456	67,456	67,456	67,456
Approved Operational Boundary	87,000	87,000	87,000	87,000

Limits to Borrowing Activity

The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. Gross external 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.

	2019-20 Original Estimate For Year End £'000	2019-20 Revised Estimate For Year End £'000	Position As At 30/09/19 £'000	2019-20 Forecast Outturn For Year End £'000
Gross borrowing	67,456	67,456	67,456	67,456
Less investments	(25,835)	(25,735)	(44,544)	(27,346)
Net borrowing	41,621	41,721	22,912	40,110
CFR (year-end position)	76,831	82,273	77,913	81,029

The Executive Director Commercialisation (Section 151 Officer) reports that no difficulties are envisaged for the current or future years in complying with this prudential indicator.

A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which 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.

Authorised limit for external debt	2019-20 Original Estimate For Year End £'000	Position As At 30/09/19 £'000	2019-20 Revised Estimate For Year End £'000
Borrowing	85,000	85,000	85,000
Other long term liabilities	1,000	1,000	1,000
Commercial activities/non-financial investments	5,000	5,000	5,000
Total	91,000	91,000	91,000

The limit of £1m for long term liabilities shown above provides headroom for the Council to take out finance leases for capital assets rather than outright purchase. Prior to taking out a finance lease, a full option appraisal would be carried out to ensure it is the most cost effective way of financing the capital expenditure.

Investment Portfolio 2019/20

In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. It is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the current 0.75% Bank Rate. The continuing potential for a re-emergence of a Eurozone sovereign debt crisis, and its impact on banks, prompts a low risk and short term strategy. Given this risk environment and the fact that increases in Bank Rate are likely to be gradual and unlikely to return to the levels seen in previous decades, investment returns are likely to remain low.

APPENDIX A

The Council held £44.554m of investments and £3.194m of loans to Welland Homes as at 30 September 2019 (£41.055m and £2.880m as at 31 March 2019). The investment portfolio yield for the first six months of the year is 1.157% against a benchmark of 0.661% (average 3 month LIBID). Deposits held excluding accrued interest were as follows:

Institution	Investment Type	Start Date	Maturity Date	Rate/Return %	As at 31-03-19 £'000	As at 30-09-19 £'000
UK Municipal Bonds Agency	Equity	n/a	n/a	n/a	50	50
Welland Homes	Equity	n/a	n/a	n/a	1,530	1,994
South Holland Community Housing Company	Equity	n/a	n/a	n/a	1,000	1,000
Lloyds Bank Current Account	Instant Access	n/a	n/a	0.65	0	112
Handelsbanken (AA)	Instant Access	n/a	n/a	0.67	1,975	4,328
CCLA Money Market Fund	Instant Access	n/a	n/a	0.73	3,000	8,070
National Westminster Bank (A+)	Certificate of Deposit	19/06/18	19/06/19	0.93	2,500	0
Lancashire County Council	Time Deposit	03/09/18	02/09/19	1.10	3,000	0
Bayerische Landesbank (A-)	Time Deposit	01/11/18	01/05/19	1.01	3,000	0
Toronto Dominion Bank (AA-)	Certificate of Deposit	07/11/18	06/11/19	1.16	2,500	2,500
Goldman Sachs International Bank (A)	Time Deposit	13/12/18	13/06/19	1.075	3,000	0
Rabobank (AA-)	Certificate of Deposit	19/12/18	18/12/19	1.14	3,000	3,000
Standard Chartered (A+)	Time Deposit	16/01/19	15/07/19	1.01	3,000	0
Credit Agricole Corporate & Investment Bank (A+)	Certificate of Deposit	31/01/19	31/01/20	1.12	3,000	3,000
Lloyds Bank (A)	Time Deposit	07/02/19	21/11/19	1.07	2,500	2,500
Australia & New Zealand Bank (AA-)	Time Deposit	27/02/19	26/02/20	1.14	2,500	2,500
Coventry Building Society (A-)	Time Deposit	27/08/19	27/02/19	0.96	3,000	0
Close Brothers (A)	Time Deposit	15/03/19	16/09/19	1.10	2,500	0
Lloyds Bank (A)	Time Deposit	12/04/19	09/04/20	1.25	0	2,500
Goldman Sachs International Bank (A)	Time Deposit	13/06/19	13/12/19	0.96	0	3,000
National Westminster Bank (A+)	Certificate of Deposit	19/06/19	17/06/20	1.00	0	5,000
Coventry Building Society (A-)	Time Deposit	29/08/19	28/02/20	0.83	0	3,000
Goldman Sachs International Bank (A)	Time Deposit	29/08/19	28/02/20	0.905	0	2,000
TOTAL					41,055	44,554

In addition to the investments listed, the Council has issued four loans to Welland Homes totalling £3.194m at a rate of 3.5% which are classified as Long Term Debtors. The Council started issuing these loans to Welland Homes in March 2017 and continued through to the present day as the housing projects have progressed.

The Executive Director Commercialisation (Section 151 Officer) confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2019/20.

The Council's budgeted investment return for 2019/20 is £519,700 (GF £358,500, HRA £161,200) and performance for the year to date is £266,187 which is broadly in line with the profiled budget. The outturn is also likely to be broadly in line with budget.

The Council monitors risk of its investment portfolio against the Link Asset Services counterparty risk matrix. This matrix gives recommended maximum investment durations for each financial institution based on the ratings allocated by the major credit rating agencies and also takes into account credit default swap prices.

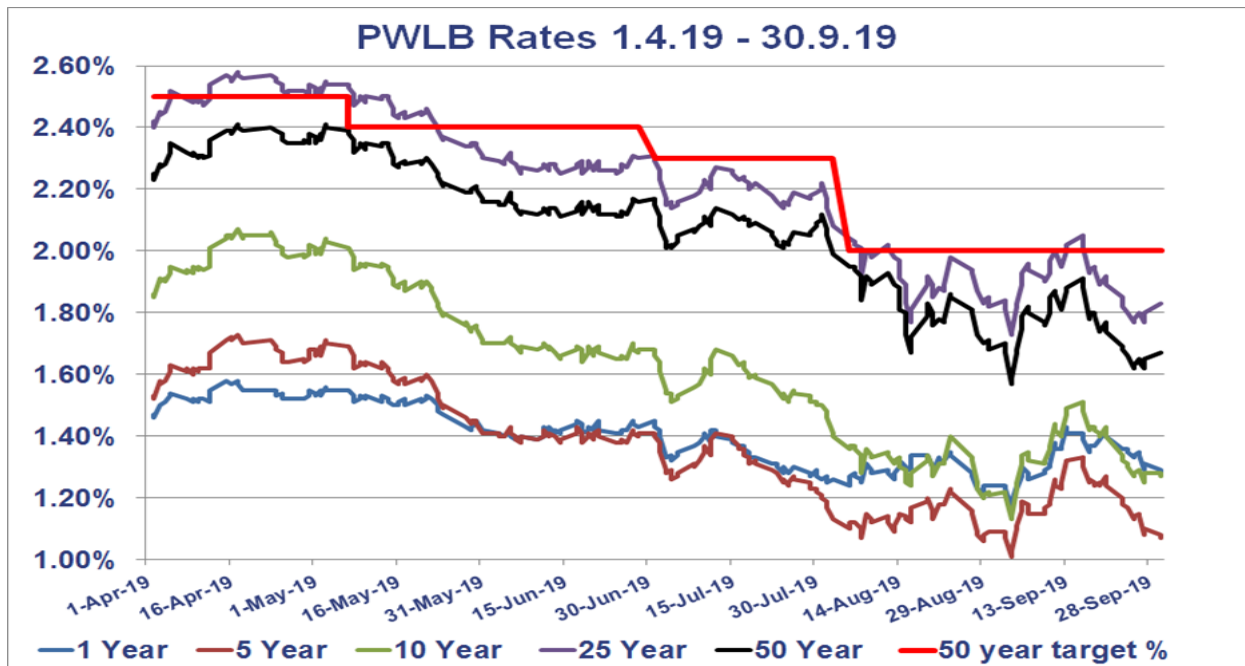
Investment Counterparty Criteria

The current investment counterparty criteria selection approved in the TMSS is meeting the requirement of the treasury management function.

Borrowing

The Council's projected capital financing requirement (CFR) for the end of 2019/20 is £81.029m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. The Council has borrowings of £67.456m in respect of the Housing Revenue Account self-financing settlement and it is anticipated that further borrowing will not be undertaken during this financial year.

The following graph shows the movement in PWLB rates for the first six months of the year to 30th September 2019:



Debt Rescheduling

The Councils external borrowing was taken out in March 2012 as part of the HRA Financing Reforms. Debt rescheduling opportunities have been very limited in the current economic climate given the consequent structure of interest rates, and following the increase in the margin added to gilt yields which has impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

In October 2019 the PWLB announced an increase of 1% on all new borrowing. This increase is across all loan periods and subsequently makes the cost of borrowing more expensive. In relation to existing borrowing, the higher rates reduces the premature repayment premium payable.

The Council's borrowing portfolio will be kept under review following these higher rates.

OTHER

Changes in risk policy

The 2018 CIPFA Codes and guidance notes have placed enhanced importance on risk management. Where an authority changes its risk policy e.g. for moving surplus cash into or out of certain types of investment funds or other types of investment instruments, this change in risk policy should be brought to members' attention in treasury management update reports.

There has been no change in risk policy to report.

UK Municipal Bonds Agency Update

The UK Municipal Bonds Agency (UKMBA) is owned by councils and the Local Government Association. South Holland DC has a £50,000 equity stake in the company.

Its aim is to offer lower cost borrowing to councils and to secure a sustainable alternative to the Public Works Loan Board for council borrowing.

The UKMBA has been working with a group of interested councils to reshape the bond offer taking on board issues that many councils have raised in relation to the joint and several liability clause. Based on this work the UKMBA undertook a tender process to select an appropriate partner to help with the restructure. This process is now complete and PFM Financial Advisors LLC (PFM) were selected.

The arrangements will be cost effective and will mean that the UKMBA will very shortly be able to offer low cost finance on terms acceptable to councils. Finance for the transition from previous arrangements to this new set up has been made available through a convertible loan from the Local Government Association. This loan recognises the importance with which this initiative continues to be viewed by the sector and confidence that the agreed changes and appointment of PFM as the service provider will deliver success.

The ability to borrow at competitive rates is vital. The UKMBA has always had the objective of beating the PWLB rate and of offering an alternative route to borrowing that could be used in the event of changes to PWLB rules. The announcement of the increase in the PWLB rate in October suggests that this route is needed now.