Appendix 1

Treasury Management Half Yearly Report – 2019/20

1. Background

The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate security and liquidity initially before considering optimising investment return (yield).

Accordingly Treasury Management is defined as:

"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

The second main function of a treasury management service is the funding of an authority's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasions any debt previously drawn may be restructured to meet Council risk or cost objectives.

2. Introduction

In February 2010 the Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Council to approve treasury management semi-annual and annual reports.

The Council's treasury management strategy for 2019/20 was approved at a meeting on 20th February 2019. The Council has invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Council's treasury management strategy.

The 2017 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 20th February 2019.

This Half Yearly Report to members is intended to provide an update of the treasury management strategy and performance for the period April to September of this financial year. It has been prepared in compliance with CIPFA's Code of Practice on Treasury Management, and covers the following:

- An economic update for the 2019/20 financial year to 30 September 2019;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy; and
- A review of the Council's investment portfolio for 2019/20.

3. Economic Update – as provided by the Council's Treasury Management Advisors, Arlingclose

UK Consumer Price Inflation (CPIH) fell to 1.7% year/year in August 2019 from 2.0% in July, weaker than the consensus forecast of 1.9% and below the Bank of England's target. The most recent labour market data for the three months to July 2019 showed the unemployment rate edged back down to 3.8% while the employment rate remained at 76.1%, the joint highest since records began in 1971. Nominal annual wage growth measured by the 3-month average excluding bonuses was 3.8% and 4.0% including bonuses. Adjusting for inflation, real wages were up 1.9% excluding bonuses and 2.1% including.

The Quarterly National Accounts for Q2 Gross Domestic Product (GDP) confirmed the UK economy contracted by 0.2% following the 0.5% gain in Q1 which was distorted by stockpiling ahead of Brexit.

Politics, both home and abroad, continued to be a big driver of financial markets over the last quarter. Boris Johnson won the Conservative Party leadership contest and has committed to leaving the EU on 31st October regardless of whether a deal is reached with the EU.

The Bank of England maintained Bank Rate at 0.75% and in its August Inflation Report noted the deterioration in global activity and sentiment and confirmed that monetary policy decisions related to Brexit could be in either direction depending on whether or not a deal is ultimately reached by 31st October.

Gilt yields remained volatile over the period on the back of ongoing economic and political uncertainty. From a yield of 0.63% at the end of June, the 5-year benchmark gilt yield fell to 0.32% by the end of September.

Recent activity in the bond markets and Public Works Loan Board (PWLB) interest rates highlight that weaker economic growth remains a global risk.

Outlook for the remainder of 2019/20

The global economy is entering a period of slower growth in response to political issues, primarily the trade policy stance of the US. The UK economy has displayed a marked slowdown in growth due to both Brexit uncertainty and the downturn in global activity. In response, global and UK interest rate expectations have eased dramatically.

Central bank actions and geopolitical risks will continue to produce significant volatility in financial markets, including bond markets.

Our treasury advisor Arlingclose expects Bank Rate to remain at 0.75% for the foreseeable future but there remain substantial risks to this forecast, dependant on Brexit outcomes and the evolution of the global economy. Arlingclose also expects gilt yields to remain at low levels for the foreseeable future and judge the risks to be weighted to the downside and that volatility will continue to offer longer-term borrowing opportunities.

	Dec 19	Mar 20	Jun 20	Sep 20	Dec 20	Mar 21	Jun 21	Sep 21	Dec 21	Mar 22	Jun 22	Sep 22	Dec 22
Official Bank Rate													
Upside Risk	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Arlingclose Central Case	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**	**0.75**
Downside Risk	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75

4. Regulatory Updates – as provided by the Council's Treasury Management Advisors, Arlingclose

Readiness for Brexit

The scheduled leave date for the UK to leave the EU is now 31st October 2019 and there remains little political clarity as to whether a deal will be agreed by this date and there is the possibility that the exit date is pushed back yet again. As 31st October approaches the Council will ensure there are enough accounts open at UK domiciled banks and Money Market Funds to hold sufficient liquidity required in the near term and that its account with the Debt Management Account Deposit Facility (DMADF) remains available for use in an emergency. The Council currently does not have any accounts outside of the UK.

5. Treasury Management Strategy Statement and Annual Investment Strategy Update

The Treasury Management Strategy for 2019/20 was approved by Full Council on 20 February 2019. The Council's annual Investment Strategy, which is incorporated in the Treasury Management Strategy, outlines the Council's investment priorities as follows:

- Security of Capital
- Liquidity

The Council will also aim to achieve the optimum return on investments commensurate with the proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term, and only invest with highly credit rated financial institutions using the Arlingclose suggested creditworthiness matrices. Currently investments are only being made with UK financial institutions.

Investments during the first six months of the 2019/20 financial year have been in line with the strategy, and there have been no deviations from the strategy.

As outlined in Section 3 above, there is considerable uncertainty in the financial and banking market, both globally and in the UK. In this context, it is considered that the strategy approved on 20 February 2019 is still fit for purpose in the current economic climate.

6. Investment Portfolio 2019/20

In accordance with the CIPFA 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. As set out in Section 3, 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 0.75% Bank Rate. Given this environment, investment returns are likely to remain low.

The Council held investments of £7.1m as at 30 September 2019; £6m was placed with three other local authorities and £1.1m was held in the Council's Lloyds Current Account. In comparison only £1.9m was held as at 31 March 2019, entirely within the Council's Lloyds Current Account.

Funds available for investment purposes can vary between nothing and £10m due to fluctuations in cash inflows and outflows during each month. Large cash inflows include council tax & business rate direct debits and the Housing Benefit subsidy from the Department for Work and Pensions. Large cash outflows include payment of the precepts to Staffordshire County Council, the Fire Authority and the Police, payment of salaries and payment of business rates to Central Government and the Staffordshire Business Rate pool.

The investment portfolio yield for the first six months of the year is 0.52%, above the target of 0.40%. The Council's budgeted investment return for 2019/20 is £49,000 (£24,500 for first 2 quarters). As at the end of the first 2 quarters of 2019/20 £23,806 of interest has been earned. Despite a slightly greater return in terms of interest rates, fewer funds have been available for investment during this period; this is expected to be the case during the rest of 2019/20.

7. Borrowing Position 2019/20

The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk and keep interest costs low. The only borrowing envisaged by the 2019/20 Treasury Management Strategy is temporary borrowing to cover short-term cash flow deficits. During the first six months of 2019/20 no borrowing has taken place.

With short-term interest rates remaining much lower than long-term rates, the Council consider it to be more cost effective in the near term to use internal resources or borrow on a short-term basis. This is also in line with advice provided by Arlingclose Ltd.

However, it was resolved at the meeting of the Council that took place on 7 September 2016, due to the delay in capital receipts; prudential borrowing will most likely be required towards the end of the 2016/17 financial year. However, this is almost certainly expected to happen during 2020/21.

8. Prudential Indicators 2019/20

Treasury management activity during the first half year has been carried out within the parameters set by the prudential indicators contained in the approved 2019/20 Treasury Management Strategy. Consequently, there is no intention to revise any of the indicators for the remainder of the year.

Annex A

Treasury Management – Glossary of Terms

- **CIPFA** – the Chartered Institute of Public Finance and Accountancy, is the professional body for accountants working in Local Government and other public sector organisations.

- **CPI** – a measure that examines the weighted average of prices of a basket of consumer goods and services. The Consumer Price Index is calculated by taking price changes for each item in the predetermined basket of goods/services and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

- **DMADF** – Debt Management Account Deposit Facility is provided by the DMO as part of its cash management operations and in the context of a wider series of measures designed to support local authorities' cash management.

- **DMO** – The Debt Management Office is an Executive Agency of Her Majesty's Treasury responsible for debt and cash management for the UK Government, lending to local authorities and managing certain public sector funds.

- **GDP** – Gross Domestic Product is the market value of all officially recognised final goods and services produced within a country in a given period of time.

- **Liquidity** – relates to the amount of readily available or short term investment money which can be used for either day to day or unforeseen expenses. For example Call Accounts allow instant daily access to invested funds.

- **MHCLG** – the Ministry of Housing, Communities and Local Government is the UK Government department for housing, communities and local government in England. Known previously as Department for Communities and Local Government (DCLG), it was renamed to add Housing to its title and changed to a ministry in January 2018.

- **PWLB** – is a statutory body operating within the United Kingdom Debt Management Office. PWLB's function is to lend money from the National Loans Fund to local authorities, and to collect the repayments.