

# **PERTH AND KINROSS COUNCIL**

**19 February 2020**

## **TREASURY ACTIVITY AND COMPLIANCE REPORT 2019/20 QUARTER 3**

**Report by Head of Finance  
(Report No. 20/48)**

### **PURPOSE OF REPORT**

The purpose of this report is to update the Council on Treasury Activity for the quarter ending 31 December 2019 and to report on compliance with the Council's Treasury Management Policy Statement (TMPS); Treasury Management Practices (TMPs); the Investment Strategy and the Prudential Indicators for the same period. The report also proposes continuation of the current Treasury Strategy, Permitted Investments and Prudential Indicators until the Council meeting on 22 April 2020.

### **1. BACKGROUND / MAIN ISSUES**

- 1.1 Treasury Management Practice 6 (TMP 6 - Reporting Requirements & Management Information Arrangements) requires that Loans Fund borrowing and investment activities are reported quarterly to the Council. This report covers the third quarter of the financial year for the period from 1 October to 31 December 2019. TMP 6 also requires that compliance with the approved TMPs, Treasury Policies and Investment Strategy are reported quarterly and this report also covers compliance for the period. The Prudential Indicators are monitored throughout the year and reported as part of the quarterly Treasury Activity and Compliance report.

### **2. ECONOMIC BACKGROUND**

- 2.1 The Bank of England Monetary Policy Committee (MPC) made no change to the Bank Base Rate of 0.75% or the quantitative easing (QE) programme of £435bn during the quarter. UK Gross Domestic Product (GDP) grew by 0.3% in the quarter to September. Growth in the service sector remained weak, with growth being the lowest since 2010.
- 2.2 During the quarter, UK unemployment in November stood at 3.8% and remained at around the lowest levels since the 1970's, whilst UK CPI inflation fell from 1.7% to 1.3% over the quarter to December. At the same time, average earnings remained above the rate of inflation. Retail sales continued to fall in November with consumers reducing spending amid Brexit and uncertainty ahead of the December election. Business investment and the housing market also slowed.
- 2.3 Internationally, Eurozone GDP growth was 0.2% in the quarter to September 2019, whilst inflation rose to 1.3% in December 2019 due to increases in energy and food costs. EU unemployment remained at 6.3% in November 2019, which was unchanged from the previous month.

- 2.4 In the US, the Federal Reserve interest rate was reduced to between 1.50% and 1.75% in October. This was the third rate cut in a year as inflation remains subdued and concerns remain about the economic outlook and ongoing trade tensions with China. The US economy grew by 2.1% annually to September 2019. Forecasts for future growth were reduced, whilst the global outlook for economic growth remained subdued.
- 2.5 The Public Works Loan Board's (PWLB) Certainty fixed interest rates for the quarter, which are based on yields on UK gilts, are shown in the graph at Appendix I. On the 9 October 2019 the UK Treasury amended its lending arrangements by increasing PWLB borrowing rates by 1%. In addition, yields rose over the quarter in response to developments with Brexit and reduced political uncertainty. PWLB rates for all borrowing periods were, therefore, higher by the end of the quarter.

### **3. TREASURY ACTIVITY**

- 3.1 A summary of the Council's treasury position and transactions is shown at Appendix II. The main activities are detailed below.
- 3.2 During the quarter there was repayment of two maturing fixed rate PWLB loans totalling £10,000,000 at an average rate of 2.98%. There was no new PWLB borrowing in this quarter due to the increase in PWLB rates, therefore the Council's total long-term debt decreased from £514M to £504M. The average interest rate on the Council's loan portfolio with the PWLB at the end of the quarter remained at 2.69%, whilst the average interest rate on all long-term debt remained at 2.85%.
- 3.3 There were three short term market loans borrowed during the quarter. The average amount was £5.8M for an average period of 28 days and at an average rate of 0.67%. Common Good and Charitable Funds held on fixed deposit within the Loans Fund remained unchanged at £2.1M with an average interest rate paid on these funds of 1.03%. Funds held from associated bodies and organisations decreased from £2.3M to £2.1M over the quarter, in line with their own cash flow requirements, whilst the average rate paid on these funds decreased from 0.18% to 0.10%, in accordance with the approved Temporary Loan policy.
- 3.4 Short term cashflow surpluses were invested in a mixture of fixed term deposits, instant access accounts, notice accounts and money market funds. All investments were made in accordance with the approved Investment Strategy and Permitted Investments.

#### Fixed Term Deposits

- 3.5 Cashflow surpluses which arise during the year and which are not immediately required are invested in fixed term deposits for periods of up to 12 months. As there was no PWLB borrowing over this quarter, the amount of fixed deposits decreased. Consequently, there were 5 fixed deposits made in the quarter, at an average amount of £4.4M, compared to 20 deposits

averaging £6.2M in the previous quarter. The average period of the deposits was 345 days, which increased slightly from 325 days in the previous quarter. The average rate achieved decreased to 1.04% in the quarter (1.09% in the previous quarter) reflecting the reduction in rates offered by the banks.

#### Investments for Daily Cashflow Requirements

- 3.6 Cashflow surpluses which arise during the year but which are required for more immediate needs, usually within the next 3 months, are invested with the Council's instant access, notice deposit accounts and money market funds. The daily average amount of such investments held over the quarter increased from £4.7M in the last quarter to £6.0M in the current quarter. The average interest rate achieved on these accounts over the quarter increased slightly from 0.78% to 0.79%.
- 3.7 All of the above investment activities are consistent with the Council's current investment strategy and cashflow requirements.
- 3.8 The total amount of investments outstanding at the end of the quarter reduced, closing at £165.2M compared to £184.9M at the end of the last quarter. The overall average rate of interest earned on the investments outstanding at the end of the quarter increased to 1.11% from 1.07% in the previous quarter. Total investment income generated on the investments undertaken during the quarter was £290,183, down from £1,333,089 earned on the investments undertaken in the previous quarter. The decrease in investment income reflects the decrease in the number of fixed deposits made in the quarter as described above. This movement reflects how investment income is reported. Income from Treasury activity is effectively shown on an annual basis, enabling the Treasury reports to separately highlight the total return on investments made in each quarter. As previously reported, the Council borrowed £115 million from the Public Works Loans Board in the period July - September last year due to historically low interest rates. This resulted in the Council having significantly more funds to invest during the last quarter and hence a much higher level of reported investment income. The movement in investment income in the current quarter, therefore, reflects the amount of new funds available to invest rather than any reduction in investment returns or the value of the Council's existing investments.

#### **4. COMPLIANCE**

- 4.1 For the quarter ending 31 December 2019, there were no breaches in compliance with the Council's approved Treasury Management Policy Statement, Treasury Management Practices (TMP's) or lending limits as detailed in TMP 4 (Approved Instruments, Methods & Techniques).
- 4.2 TMP4 also requires that a working list of specific approved counterparties (including lending limits) is maintained by the Head of Finance and continuously reviewed and updated for any movements in credit ratings and other factors including press coverage or emerging issues. The Council's Treasury advisor's (Link Asset Services) suggested maximum lending period

for each counterparty is also included within the Council's approved lending policy, where appropriate. Appendix III shows the list of approved counterparties, based on the current lending policy, as at January 2020.

- 4.3 A further requirement of TMP4 is to measure cashflow performance, which is expressed as the average closing cleared bank balance for the period. For the quarter ending 31 December 2019 the average closing cleared bank balance was £5,544.41 in credit. This is within the set target range of £50,000 (debit or credit).

## **5. INVESTMENT STRATEGY COMPLIANCE AND PERFORMANCE**

- 5.1 The Treasury Investment Strategy for 2019/20 approved by the Council at its meeting on 27 February 2019 (Report No.19/59 refers) sought to ensure security over principal sums invested, whilst obtaining optimum returns consistent with this approach. Therefore, the only Permitted Investments are in low risk organisations. Revised individual counterparty limits were approved by the Council at its meeting on 25 September 2019 (report 19/277 refers). The limits for each Permitted Investment and individual counterparty ensure a spread of investments, thereby also spreading any risk. The Council needs to ensure sufficient liquidity at all times to meet its obligations as they fall due and consequently investments must be made in accordance with cashflow requirements. The approved Strategy was based on the assumption that the level of investments would increase in the first half of the year, however, they were not expected to exceed £80,000,000 unless new borrowing was undertaken early in the year.
- 5.2 The level of investments fluctuated over the quarter and peaked at £203.675M on 16 October 2019. This balance reflects the impact of the PWLB borrowing undertaken over the previous quarter and will steadily reduce over the next 2 years in line with delivery of the Council's Capital Programme. The average daily investment balance over the quarter was £191.0M, which increased from an average of £138.1M in the previous quarter, and increased from £60.1M in the same quarter of last year.
- 5.3 The Investment Strategy was applied in full over the quarter, with liquidity being maintained by the use of instant access accounts, notice accounts and money market funds as detailed in Section 3.6 above. There were no other risks identified in the quarter.
- 5.4 The Investment Strategy also incorporates investments held by the Common Good Funds. All such investments during the quarter were with the Council's Loans Fund, in line with the approved Strategy. The only Council funds held by external fund managers relate to Council administered Charitable Trusts and are, therefore, not covered by this Investment Strategy.
- 5.5 The Annual Property Investment Strategy for 2019/20 was also approved by the Council at its meeting on the 27 February 2019 and has been complied with in full, with no breaches in compliance with Permitted Investment limits.

- 5.6 The budgeted income in 2019/20 for Commercial Property investments was originally projected to be £1,836,000 and has subsequently been increased to £1,922,000. Projections for 2019/20 have been obtained from the Council's Corporate Property system.
- 5.7 There were neither additional risks identified nor new property investments entered into during the quarter. The Strategy action plan for the rationalisation of the commercial property portfolio remains on programme.

## **6. PRUDENTIAL INDICATORS**

- 6.1 The Council approved Prudential Indicators for 2019/20 to 2028/29 as part of the Treasury & Investment Strategy (Report No. 19/59 refers). These indicators are based on the approved Composite Capital Budget and the Housing Investment Programme.
- 6.2 The latest estimates of the Prudential Indicators, in line with the Council's current approved Capital Budget and Capital Financing (borrowing) Requirements, are shown at Appendix IV.
- 6.3 The indicator for Financing Costs remains at a relatively low level as a result of continuing low interest rates, as well as pro-active treasury management. Consequently, they only fluctuate each year within a narrow range, reflecting a stable budgetary position. However, Financing Costs are on a gradually increasing trend as interest rates are anticipated to rise over the coming years, coupled with the estimates now including the increase in interest rates offered by the PWLB. The movements in estimated Capital Expenditure and the Capital Financing Requirement reflect movements on the Composite Capital and Housing Investment programmes approved by the Strategic Policy & Resources Committee.
- 6.4 All Indicators remain within their current and projected estimates and limits, and accordingly all Prudential Limits were complied with throughout the period. Overall, the Council's plans remain affordable, prudent and sustainable over the medium term.

## **7. UPDATED TREASURY STRATEGY AND PRUDENTIAL INDICATORS**

- 7.1 The Council is due to consider the setting of a new 10-year Capital Budget for 2020/21 to 2029/30 at the special Council meeting on 4 March 2020. Once the new Capital Budget has been approved, the Council's Treasury Strategy, including Permitted Investments, and Prudential Indicators for the forthcoming financial year would be formulated and considered by the Council at its next meeting, which should be before the start of the new financial year on 1 April. However, the next meeting of the Council is not scheduled until 22 April 2020.
- 7.2 Consequently, it is proposed that the current approved Treasury Strategy, including Permitted Investments, and the Prudential Indicators continue in place beyond 31 March 2020 until the revised Strategy, Permitted

Investments and Prudential Indicators are considered by the Council at its meeting on 22 April 2020.

## **8. CONCLUSION AND RECOMMENDATIONS**

- 8.1 UK GDP grew by 0.3% in the 3 months to September, whilst CPI inflation fell over the quarter to 1.3%. Unemployment levels remained low, whilst average earnings remained above inflation for the quarter. The Bank of England's Monetary Policy Committee made no change to the Bank Base Rate of 0.75%. There was less volatility in the financial markets over the quarter, as a result of Brexit developments, the UK Parliamentary election in December and other global economic developments. During the quarter PWLB rates increased accordingly.
- 8.2 Activities in the quarter included repayment of maturing long-term PWLB loans, with no new borrowing undertaken. Consequently, investment activity decreased in comparison to the previous quarter. Instant access notice accounts and money market funds were used to meet short term liquidity requirements. The level of investments decreased over the quarter in line with expectations.
- 8.3 The Council adhered to its Investment Strategy and policies throughout the quarter, with no breaches in compliance.
- 8.4 It is recommended that the Council:
1. Notes the content of this report, which is submitted in accordance with the Council's approved Treasury Management Practices.
  2. Approve the continuation of the current approved Treasury Strategy, Permitted Investments and Prudential Indicators until the next meeting of the Council scheduled for 22 April 2020 as outlined at Section 7.

### **Author(s)**

<b>Name</b>	<b>Designation</b>	<b>Contact Details</b>
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### **Approved**

<b>Name</b>	<b>Designation</b>	<b>Date</b>
Stewart MacKenzie	Head of Finance	6 February 2020
Jim Valentine	Depute Chief Executive (Chief Operating Officer)	6 February 2020

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## 1. IMPLICATIONS, ASSESSMENTS, CONSULTATION AND COMMUNICATION

<b>Strategic Implications</b>	<b>Yes / None</b>
Community Plan / Single Outcome Agreement	None
Corporate Plan	Yes
<b>Resource Implications</b>	
Financial	Yes
Workforce	Yes
Asset Management (land, property, IST)	Yes
<b>Assessments</b>	
Equality Impact Assessment	Yes
Strategic Environmental Assessment	Yes
Sustainability (community, economic, environmental)	Yes
Legal and Governance	None
Risk	None
<b>Consultation</b>	
Internal	Yes
External	None
<b>Communication</b>	
Communications Plan	None

### 1. Strategic Implications

#### Corporate Plan

1.1 The Council's Corporate Plan 2013 – 2018 lays out five outcome focussed strategic objectives which provide clear strategic direction, inform decisions at a corporate and service level and shape resources allocation. They are as follows:

- (i) Giving every child the best start in life;
- (ii) Developing educated, responsible and informed citizens;
- (iii) Promoting a prosperous, inclusive and sustainable economy;
- (iv) Supporting people to lead independent, healthy and active lives; and
- (v) Creating a safe and sustainable place for future generations.

1.2 This report relates to all of these objectives.

### 2. Resource Implications

#### Financial

2.1 There are no direct financial implications arising from this report other than those reported within the body of the main report.

### Workforce

- 2.2 There are no direct workforce implications arising from this report.

### Asset Management (land, property, IT)

- 2.3 There are no direct asset management implications arising from this report other than those reported within the body of the main report.

## **3 Assessments**

### Equality Impact Assessment

- 3.1 Under the Equality Act 2010, the Council is required to eliminate discrimination, advance equality of opportunity, and foster good relations between equality groups. Carrying out Equality Impact Assessments for plans and policies allows the Council to demonstrate that it is meeting these duties.
- 3.2 The information contained within this report has been considered under the Corporate Equalities Impact Assessment process (EqIA) and has been assessed as **not relevant** for the purposes of EqIA.

### Strategic Environmental Assessment

- 3.3 The Environmental Assessment (Scotland) Act 2005 places a duty on the Council to identify and assess the environmental consequences of its proposals.
- 3.4 The information contained within this report has been considered under the Act. However, no action is required as the Act does not apply to the matters presented in this report.

### Sustainability

- 3.5 Under the provisions of the Local Government in Scotland Act 2003 the Council has to discharge its duties in a way which contributes to the achievement of sustainable development. In terms of the Climate Change Act, the Council has a general duty to demonstrate its commitment to sustainability and the community, environmental and economic impacts of its actions.
- 3.6 The information contained within this report has been considered under the Act. However, no action is required as the Act does not apply to the matters presented in this report.

## **4. Consultation**

- 4.1 The Chief Executive, and the Council's Treasury advisors, Link Asset Services, have been consulted in the preparation of this report.



## **2. BACKGROUND PAPERS**

- 2.1 No background papers, as defined by Section 50D of the Local Government (Scotland) Act 1973 (other than any containing confidential or exempt information) were relied on to any material extent in preparing the above report.

## **3. APPENDICES**

- Appendix I – PWLB Fixed Maturity Interest Rates from 1 October to 31 December 2019.
- Appendix II – Summary of the Treasury Position and Transactions from 1 October to 31 December 2019.
- Appendix III – Approved Investment Counterparty List
- Appendix IV – Monitoring of Prudential Indicators – Quarter-ending 31 December 2019