



DECISION PAPER

DECISION: 2018/41	DATE: 5TH DECEMBER 2018
TITLE: Treasury Management mid-year report 2018/19	
REPORT BY: Steve Freeman, Chief Finance Officer	

Executive Summary

In accordance with the CIPFA Treasury Management code of practice and to strengthen oversight of the PCC's treasury management activities, the PCC will receive updates on treasury management issues including a mid-year report. This report provides information on treasury management activity that has been undertaken in the current financial year and reports on the overall performance against the agreed strategy and prudential indicators.

Recommendations

The Police and Crime Commissioner is asked to note the report.

Signature

Police and Crime Commissioner

Date

5th December 2018

PART I

POLICE & CRIME COMMISSIONER FOR LANCASHIRE

REVIEW OF TREASURY MANAGEMENT 2018/19 Mid-Year Report

Economic Overview

During the period, economic growth has continued to be positive, albeit at historically low levels, and unemployment is low with the Bank of England projecting that it will fall a little further. At the same time, inflation has remained above the Bank of England's 2% target rate. In August the CPI rose to 2.7%. As a consequence of these economic factors, in August the Bank of England's Monetary Policy Committee (MPC) voted unanimously to increase Bank Rate by 0.25% to 0.75%.

Internationally, the US economy has continued to grow and at their meeting in September the central bank increased interest rates for the third time in 2018. In Europe the level of growth has moderated after a period of strong growth.

There is still a lot of uncertainty over the economy much of it arising from political factors. Domestically, the progress and unknown impact of the UK's withdrawal from the European Union continues to dampen investment. On the world economy the period has seen an increase in the potential for a trade war between the USA and China. Economic problems in Turkey and Argentina are also causing concern in international markets.

Outlook for Interest Rates

The Bank of England has raised expectations of gradual increases in interest rates and the increase in August was part of this. It is expected that this trend will continue. This is reflected in the County Council's Treasury advisers Arlingclose forecast for interest rates. Their central forecast sees a further 0.25% increase in March and September 2019 which would take the bank rate to 1.25%. They anticipate the rate would then stay constant up to September 2021 which is the end of the forecast period. However, with the current economic data and the risks in the economy they consider that there are also downside risks to the forecast.

The table below shows Arlingclose, latest forecast for interest rates

Period	Bank Rate	3 month money market	12 month money market	20-year Gilt Rate
Q4 2018	0.75	0.8	1.05	1.9
Q1 2019	1.0	1.0	1.25	1.95
Q2 2019	1.0	1.1	1.35	1.95
Q3 2019	1.25	1.2	1.4	2.0
Q4 2019	1.25	1.3	1.5	2.0
Q1 2020	1.25	1.3	1.45	2.0
Q2 2020	1.25	1.25	1.4	2.0
Q3 2020	1.25	1.2	1.4	2.0
Q4 2020	1.25	1.2	1.4	2.0
Q1 2021	1.25	1.2	1.4	2.0
Q2 2021	1.25	1.2	1.4	2.0
Q3 2021	1.25	1.2	1.4	2.0
Q4 2021	1.25	1.2	1.4	2.0

Treasury Management position and Policy

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The treasury management activity is influenced both by the position at the beginning of the year and the plans in year. The position at the start of the financial year is summarised in the Table below:

	Balance
	31.3.18
	£m
Capital Finance Requirement	57.825
External borrowing	22.527
Reserves	38,946
Working capital	1,908
Available for investment	40,854
Investments	6,562

The table above shows that the level of loans was below the CFR at 31.3.18 and the investments held are below the available reserves. This reflects the policy followed by the Authority of using cash balances to finance the capital expenditure as it is estimated that the cost of borrowing exceeds the income that would be made on the investments.

In accordance with this policy the Commissioner has not borrowed for capital purposes since 2007. However at the start of the year it was anticipated that with the proposed borrowing requirement of £6.4m in the Capital Programme and the falling level of reserves that this would not be sustainable. The expectation was that some borrowing may be required although it was likely to be kept to a minimum by the continued use of internal borrowing. The 2018/19 Treasury Management Strategy states "The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. Continuing the policy of using internal balances is likely to increase the need for the Commissioner to incur short term loans to cover cash flow shortages."

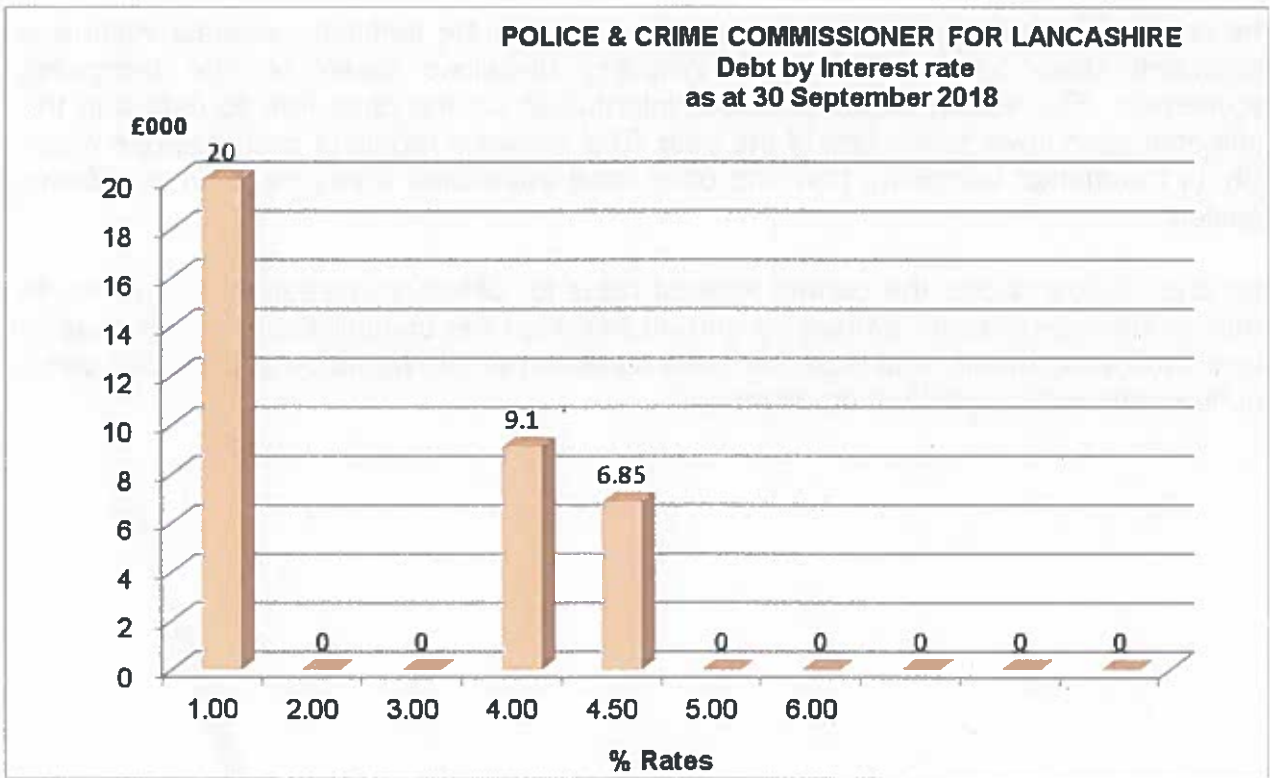
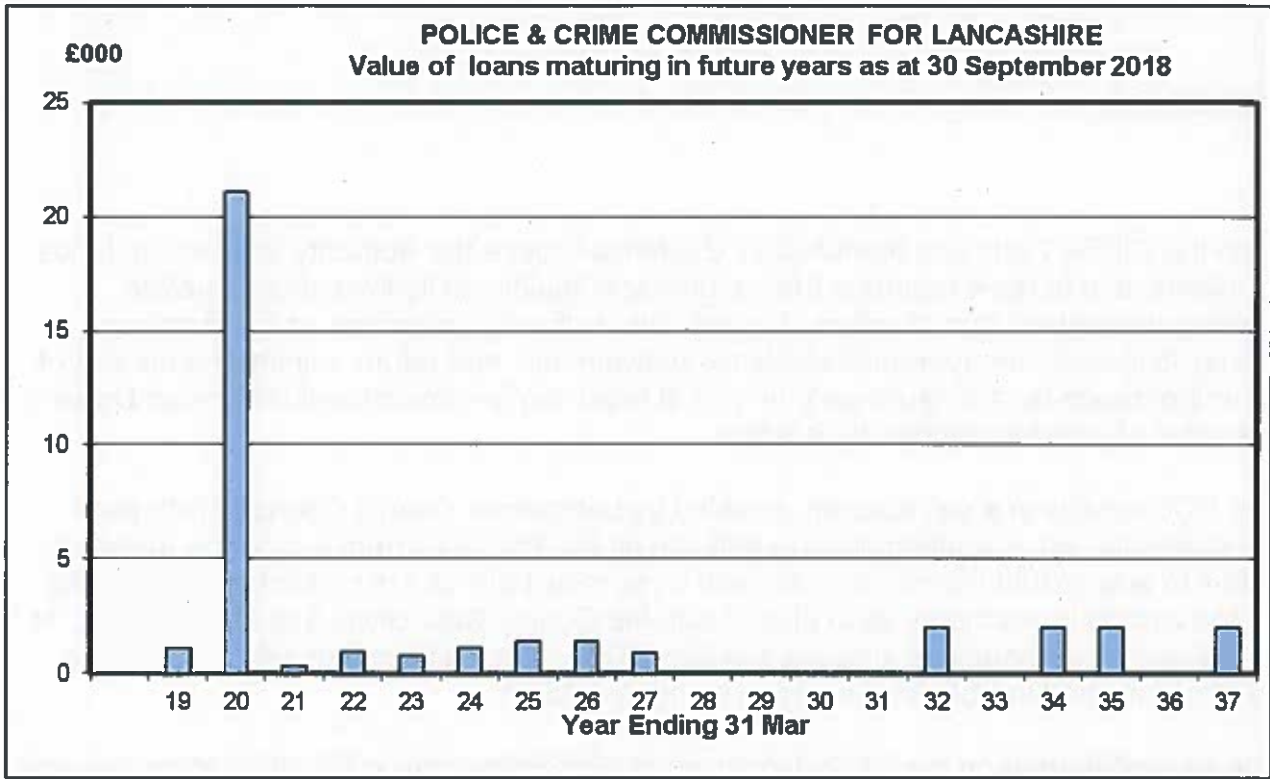
Borrowing

Existing borrowing is principally with the Public Loans Work Board and at 1 April the debt outstanding was £17.054mm. To date no new borrowing from the PWLB has been taken in the year while in September a maturing debt of £1.1m was repaid. At the beginning of the year the commissioner also had a £5m loan with a local authority which matured on 12 September 2018 and transferred debt of £0.473 giving total debt of £22.527m

As anticipated in the strategy the PCC has required some borrowing in the year. It is considered that short term loans represent the best value for money therefore the following loans with other local authorities have been taken in the year.

Amount	Start date	Maturity date	Interest rate (%)
£5,000,000	16 April 2018	15 April 2019	1.00
£5,000,000	27 April 2018	26 April 2019	1.04
£5,000,000	23 May 2018	5 April 2019	0.74
£5,000,000	27 June 2018	8 April 2019	0.70

Therefore the debt at 30.9.18 is £36.427m. The charts below show the current maturity profile of the Commissioner's borrowings, along with an analysis of the debt by interest rate.



Investments

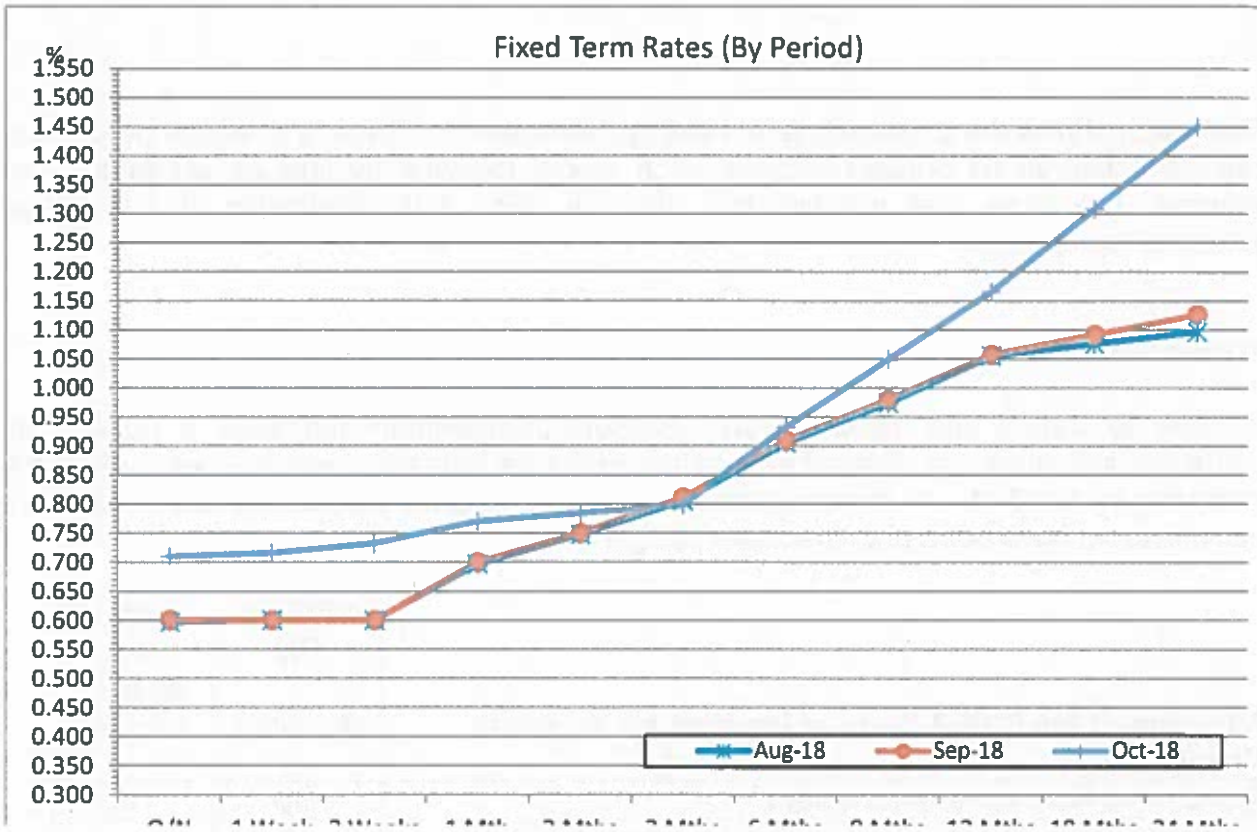
Both the CIPFA Code and the MHCLG Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving low investment returns and having the value of reserves eroded by inflation.

The PCC invests in a call account provided by Lancashire County Council which pays the base rate. Each working day the balance on the PCC's Current Account is invested in this to ensure that the interest received on surplus balances is maximised. During the period all new investments were placed with the County Council via this arrangement. At 30th September there was a balance of £36.257m in the call account with the average balance invested in LCC for the period being £34.068m.

The interest earned on the call balances as at 30th September is £0.107m at an average rate of 0.62%. This compares favourably with the benchmark 7 day LIBOR index which averages 0.56% over the same period.

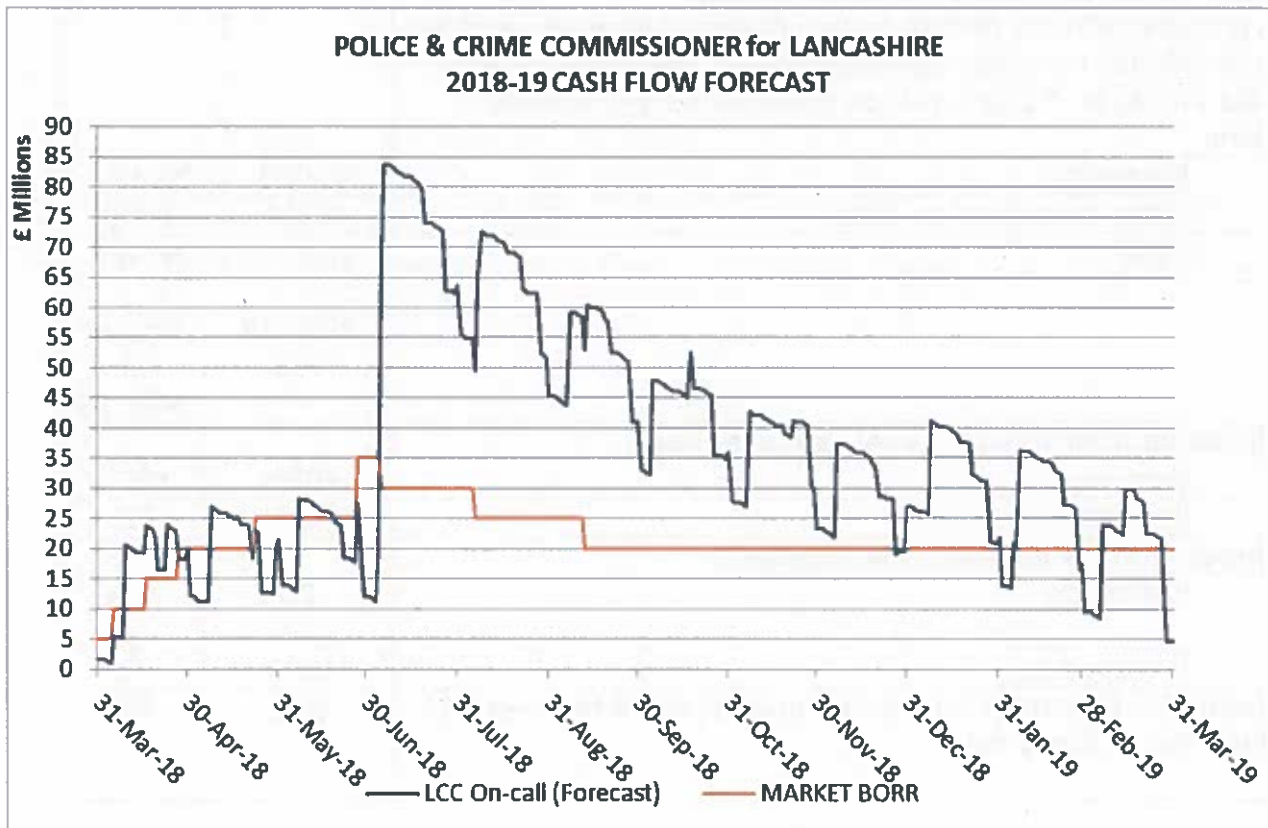
The opportunity to fix investments longer term to generate additional interest income is dependent upon future cash flows including decisions taken on the borrowing requirement. The section below provides information on the cash flow to date and the estimated cash flows to the end of the year. This shows a reducing cash balance which without the market borrowing from the other local authorities would be in an overdrawn position.

The chart below shows the current interest rates for different investment maturities. In order to increase the rate earned on current balances the commissioner would need to place fixed investments of at least 3 months duration but this would be dependent upon a counter party with a sufficient credit rating.



Cash Flow

The estimated cash flow totals are as follows:



This graph shows the total cash level held by the Authority. There is a regular pattern as cash is bolstered by precept receipts each month followed by falls as expenditure is incurred. The large cash injection from the low point at the beginning of July is the pensions top up grant.

Prudential Indicators

In order to control and monitor PCC's treasury management functions, a number of prudential indicators are determined against which performance may be measured. The indicators for 2018/19 are shown in the table below alongside the current actual. None of the indicators have been breached over the period.

	2018-19 PIs	Actual at 30.9.18
Adoption of the CIPFA Code of Practice for Treasury Management	Adopted	Adopted
Authorised limit for external debt	£m	£m
A prudent estimate of total external debt, which does not reflect the worst case scenario, but allows sufficient headroom for unusual cash movements		
Borrowing	63.000	36.427
Other long-term liabilities	1.000	0.000
Total	64.000	36.427
Operational boundary for external debt		
A prudent estimate of debt, but no provision for unusual cash movements. It represents the estimated maximum external debt arising as a consequence of the Authority's current plans		
Borrowing	45.000	36.427
Other long-term liabilities	0.500	0.000
Total	45.500	36.427

	2016-17 PIs	Actual at 30.9.16
Upper limit for fixed interest rate exposure		
Borrowing	100%	100%
Investments	100%	0
Upper limit for variable rate exposure		
Borrowing	75%	0%
Investments	100%	100
Upper limit for total principal sums invested for over 364 days (per maturity date)	50%	Nil

Maturity structure of debt from 31.3.18	Upper/ Lower Limits	Actual
Under 12 months	70% / nil	1%
12 months and within 24 months	60% / nil	58%
24 months and within 5 years	65% / nil	6%
5 years and within 10 years	80% / nil	13%
10 years and above	90% / 10%	22%

Regulatory Updates

Prudential and Treasury Management Codes

CIPFA has introduced updated versions of the Prudential and Treasury Management Codes. In addition the MHCLG has re-written its Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return. This will cover commercial activity and loans to employees. The PCC will need to consider its Capital Strategy and Investment Strategy for 2019/20 having regard to these documents.

Business Risk Implications

The Treasury Management strategy is designed to minimise the PCC for Lancashire's financial risk associated with investment decisions, whilst maximising the return on any investments made. As such the adoption of the CIPFA's Code of Practice on Treasury Management and the monitoring arrangements in place ensure that any risks faced by PCC are managed.

However, it must be acknowledged that there will always be a balance between risk and return and hence the strategy does not completely eliminate the risk of any further default on investments in the future.

1. Links to the Police and Crime Plan

2. Consultation

3. Implications

a. Legal

There are no legal comments associated with this paper.

b. Financial

The financial implications are contained in the report

c. Equality considerations

There are no Equality comments associated with this paper.

4. Background Papers

CIPFA Treasury Management Code of Practice
PCC for Lancashire Treasury Management Strategy 2018/19

5. Public access to information

Information in this form is subject to the Freedom of Information Act 2000 and other legislation.

Part 1 of this form will be made available on the PCC website within 3 working days of approval. Any facts/advice/recommendations that should not be made available on request should not be included in Part 1 but instead on the separate Part 2 form.

Officer declaration	Date
LEGAL IMPLICATIONS – As above	
FINANCIAL IMPLICATIONS – As above	
EQUALITIES IMPLICATIONS – As above	
CONSULTATION – As above	
<p data-bbox="150 725 1278 761">Director to the Office of the Police and Crime Commissioner (Monitoring Officer)</p> <p data-bbox="150 792 1353 927">I have been informed about the proposal and confirm that financial, legal and equalities advice has been taken into account in the preparation of this report. I am satisfied that this is an appropriate request to be submitted to the Police and Crime Commissioner for Lancashire.</p> <p data-bbox="150 994 1166 1028">Signature.....Date.....</p>	

