WOKINGHAM BOROUGH COUNCIL

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Treasury Management

Mid-Year Treasury Management Report 2017-18

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1. Introduction

This report presents the Council's mid-year treasury position for 2017-18 in accordance with the Council's treasury management practices.

It explains the current economic environment expectations for the near future. It then analyses the latest analysis of capital expenditure which is a key driver of treasury management, driving the borrowing requirement of the organisation. It then shows how the Council has financed its borrowing between internal and external borrowing and then how the Council has managed its short-term cash investments.

The Council's treasury management strategy is largely influenced by capital expenditure. Revenue expenditure is largely balanced with expenditure matching income, and short term borrowing and deposits. The large driver of the longer term treasury management strategy is therefore capital expenditure and financing.

There are two aspects of treasury performance – debt management and cash investment:

- debt management relates to the Council's borrowing;
- cash investment relates to the investment of surplus cash balances.

2. The Economy and Interest Rates forecast

Following strong UK economic growth in 2016, growth in 2017 has been more weak; with quarterly growth at just 0.3%, meaning that growth in the first half of 2017 was the slowest since 2012. This has largely been caused by the sharp increase in inflation, caused by the devaluation of sterling after the referendum, increasing the cost of imports.

As a result, on the second of November, the official bank rate was lifted from 0.25% to 0.5%, the first increase since July 2007. The monetary policy committee also expect the bank rate to increase twice more in the next three years to reach 1% by 2020.

Economic forecasting remains difficult with so many external influences weighing on the UK. The overall longer run trend is for PWLB rates to rise, albeit gently.

The Council's treasury advisor, Link Asset Services (formerly Capita Asset Services), has provided forecasts for PWLB rates based on the certainty rate (minus 20 bps) which has been accessible to most local authorities since 1 November 2012, as shown in table 1, below.

Table 1: Interest rate forecasts for bank rate and PWLB

	Now	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19
Bank Rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	0.75%	0.75%	0.75%	1.00%
5yr PWLB rate	1.50%	1.50%	1.60%	1.60%	1.70%	1.80%	1.80%	1.90%	1.90%	2.00%
10yr PWLB rate	2.10%	2.10%	2.20%	2.30%	2.40%	2.40%	2.50%	2.50%	2.50%	2.70%
25yr PWLB rate	2.70%	2.80%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%
50yr PWLB rate	2.40%	2.50%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%

The November inflation report included an increase in the peak forecast for inflation from 3.0% to 3.2% very soon, with a slow decrease in the inflation rate to just over the 2% target in three years' time.
Chancellor Phillip Hammond will announce his new budget on November 22, the first since the general election, which will be important, as the Government begins to implement its revised target of achieving a budget surplus by 2025, eased from 2020 previously.

3. The Council's Capital Expenditure and Financing 2017/18

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- financed in year, immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need or;
- funded by borrowing (internal or external).

The actual capital expenditure forms one of the required prudential indicators. Tables 2 and 3 below show the actual capital expenditure and the funding.

Table 2: General fund capital expenditure and financing	2017/18 Budget	Quarter 1 17/18 Year end forecast	Quarter 2 17/18 Year end forecast
Capital expenditure	£'000	£'000	£'000
Financed in year	70,322	54,499	45,790
Funded by borrowing (borrowing requirement)	82,527	64,444	48,347
Total	152,849	118,943	94,137*

Note:* Slippage in the delivery of the capital programme has resulted in this reduction

Table 3: HRA capital expenditure and financing	2017/18 Budget	Quarter 1 17/18 Year end forecast	Quarter 2 17/18 Year end forecast
Capital expenditure	£'000	£'000	£'000
Financed in year	5,100	5,100	5,100
Funded by borrowing (borrowing requirement)	0	0	0
Total	5,100	5,100	5,100

4. The Council's Overall Borrowing Need

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). It represents the 2017/18 capital expenditure financed by borrowing, and prior years' unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

The Council's general fund underlying borrowing need (CFR) is not allowed to rise indefinitely. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision (MRP), to reduce the CFR. This ensures the general fund pays for the capital asset and is a proxy for depreciation. The total CFR can also be reduced by:

- The application of additional capital financing resources (such as unapplied capital receipts); or
- An additional revenue contribution to the statutory minimum revenue provision (MRP) each year through a Voluntary Revenue Provision (VRP).

This differs from the treasury management arrangements which relates to cash transfers. External debt can be borrowed or repaid at any time, but this does not change the CFR.

The Council's CFR forecast for 2017/18 year end is shown below, and represents a key prudential indicator. It includes PFI and leasing schemes on the balance sheet, which increase the Council's borrowing need. However no borrowing is actually required against these schemes as a borrowing facility is included in the contract.

Table 4: Capital financing requirement: General Fund	**2017/18 Budget**	**Quarter 1 17/18 Year end forecast**	**Quarter 2 17/18 Year end forecast**
Opening balance £'000*	**119,013**	**160,022**	**160,022**
Capital expenditure funded by Borrowing	**82,527**	**64,444**	**48,347**
Sub Total	**201,540**	**224,467**	**208,369**
Less Minimum Revenue Provision			
MRP Charge	**(3,350)**	**(3,090)**	**(3,024)**
PFI Principal Charge	**(215)**	**(215)**	**(215)**
Sub Total	**(3,565)**	**(3,305)**	**(3,239)**
Closing Balance	**197,975**	**221,162**	**205,130**
Movement		**61,140**	**45,108**

Note: * The opening balance for the budget was an estimate as at Jan 2017. The Actual closing balance for 2016/17 was higher than forecast, this has resulted in a higher 2017/18 opening balance.

Table 5: Capital financing requirement: HRA

	2017/18 Budget	Quarter 1 17/18 Year end forecast	Quarter 2 17/18 Year end forecast
Opening balance	90,400	90,400	90,400
Capital expenditure funded by Borrowing	0	0	0
Closing Balance	90,400	90,400	90,400
Less Minimum Revenue Provision			
Repayment of Loan Principle	(1,750)	(2,548)	(2,548)
PFI Principal Charge	0	0	0
Sub Total	(1,750)	(2,548)	(2,548)
Closing Balance	88,650	87,852	87,852
Movement		2,548	2,548

Table 6: Capital financing requirement: General fund and HRA

	2017/18 Budget	Quarter 1 17/18 Year end forecast	Quarter 2 17/18 Year end forecast
Opening balance £'000	209,413	250,422	250,422
Capital expenditure funded by Borrowing	82,527	64,444	48,244
Sub Total	291,940	314,867	298,769
Less Minimum Revenue Provision			
MRP Charge	(5,100)	(5,638)	(5,572)
PFI Principal Charge	(215)	(215)	(215)
Sub Total	(5,315)	(5,853)	(5,787)
Closing Balance	286,625	309,014	292,982
Movement		58,592	42,560

Note: All borrowing is within are authorised limits.

The capital expenditure funded by borrowing requirement includes the funding of the following:

- Town centre regeneration
- Loans to group companies
- Forward funded schemes

The above borrowing will be reduced when capital receipts are recovered, loans repaid and when developer contributions are received.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. The Council does not borrow all of this money externally but uses some of its internal cash reserves to fund this expenditure. This is referred to as "internal borrowing". This means that the Council's capital financing requirement is higher than its external borrowing figures. External borrowing may be sourced from bodies such as the Public Works Loan Board (PWLB) or the money markets.

5. External borrowing and compliance with treasury limits and prudential indicators

Table 7, below, demonstrates the current and forecast 2017/18 external borrowing.

Table 7: External Borrowing

	Actuals as at 30-09-17	Quarter 1 17/18 Year end forecast	Quarter 2 17/18 Year end forecast
	£'000	£'000	£'000
Market	24,000	24,000	24,000
PWLB*	122,459	120,709	120,709
Local Enterprise Partnership**	1,380	1,000	1,000
Total borrowing	147,839	145,709	145,709

Note:* reduction due to a HRA self-financing loan repayment
Note: reduction due to a Local Enterprise Partnership loan repayment**

During the first six months of the 2017/18 financial year, the Council operated within the treasury limits as set out in treasury management strategy. The position for the treasury management prudential indicators is shown on the following page in table 8, below. These show that all prudential indicators have been complied with. Further detail on each of these indicators is included in Appendix B.

Table 8: Prudential Indicator – Debt

Forecast year-end position as at 30-09-17	Has the limit/boundary been broken
Gross external borrowing exceeding CFR	NO
Authorised limit	NO
Operational boundary for external debt	NO
HRA debt limit	NO
Maturity structure of borrowing	NO
Upper limits on interest rate exposure	NO
The percentage of financing costs set aside to service debt financing costs	NO

Note: prudential indicators is shown in table 8 and full details are available in appendix B.

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 (plus the estimates of any additional capital financing requirement for the current 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.

6. Compliance with treasury limits and prudential indicators for investments

The treasury management team ensure the cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering maximising investment return. The return on investments contributes to the Council's budget for both the general fund and housing revenue account.

Table 9, below, shows the counterparties where cash deposits are held. Further detail is available in appendix D.

Table 9: Investment Type	Quarter 1 Actuals invested	Quarter 2 Actuals invested
	£'000	£'000
Local authorities	60,000	63,000
Money market funds	3,500	0
Fund managers	631	631
Internal companies investments (including the HRA)	26,359	30,091
Total	90,490	93,722

During the first six months of the 2017/18 financial year the Council operated within the treasury limits as set out in investment strategy. The position for the investment prudential indicators is shown in table 10 and full details are available in appendix B.

Table 10: Investments return	Quarter 1 Forecast outturn	Quarter 2 Forecast outturn
	£'000	£'000
Local authorities	206	434
Money market funds	5	9
Fund managers	0	0
Internal Companies investments (including the HRA)	1,308	1,608
Total	1,519	2,051

Current forecast of investment return shows we will over achieve the budget (Budget £1,451,000 year end outturn forecast as ate September is £1,790,000). This is due to loans made to our housing companies.

7. Conclusion

The Director of Corporate Services confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2017/18 and that no difficulties are envisaged for the remaining six months in complying with the prudential indicators. The Council is operating in a stringent financial climate, but

is still managing to deliver within budgeted interest levels.

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