WOKINGHAM BOROUGH COUNCIL

Treasury Management

Treasury Management Strategy Report 2019-20

Contents

Appendices

1. Introduction

This report presents the Council's Treasury Management Strategy for 2019-20 in accordance with the Council's Treasury Management practices.

The Council is required to receive and approve three main reports each year, which incorporate a variety of policies, estimates and actuals. These are the Treasury Management Strategy (this report), the Treasury Management mid-year report and finally the annual outturn treasury report:

Treasury Management Strategy:

The first and most important report covers:

- The treasury management strategy ***-How the investments and borrowings are to be organised*** including treasury indicators
- An investment strategy -***The criteria on how investments are to be managed and the limitations including investment in assets***
- The capital plans (including prudential indicators)
- A minimum revenue provision (MRP) policy ***-How outstanding borrowing in respect of capital expenditure is repaid by charges to revenue over time***

Treasury Management mid-year report

This report updates members with the progress of the capital position, amending prudential indicators as necessary, and confirming whether the treasury strategy is being complied with or whether any policies require revision.

Annual Treasury report

This report, which is produced following the year-end provides details of a selection of actual Prudential and Treasury indicators and actual Treasury operations compared with the estimates within the strategy.

Training

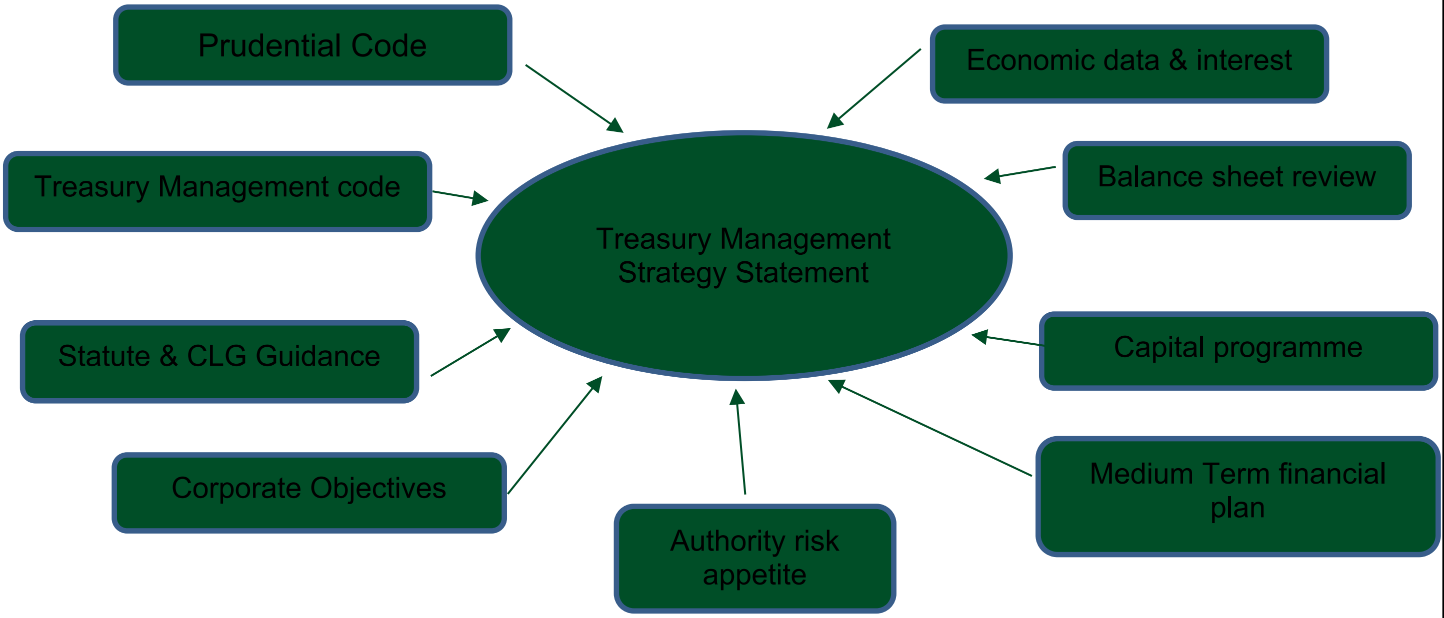
The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. Training for members will be arranged in the period covered by this report.
The training needs of treasury management officers are periodically reviewed.

Treasury management consultants

The Council uses Link Asset Services Treasury Solutions (LAS TS) as its external treasury management advisors. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers. It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

2. Treasury management policy statement

Factors that shape the Treasury Strategy



Wokingham Borough Council Treasury Management Policy Statement for 2019/20 is:

- The Council defines it's treasury management activities as:
    - the management of the Council's investments and cash flows, banking, money market and capital market transactions,
    - the effective control of the risks associated with above mentioned activities and,
    - The pursuit of optimum performance consistent with those risks.

- The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council.

- The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving best value in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

3. The Economy and Interest Rates forecast

World update

Most European stocks rose to near two month highs on the 25-01-19, following gains on Wall Street the day before, and further helped by US Treasury Secretary saying that the US and China were "making a lot of progress" on trade talks, The DAX and CAC close 1.4% and 1.1% higher respectively. By contrast the FTSE dipped by 0.1% to post a fourth successive negative session dragged lower by Vodafone, which stumbled to an eight and a half year low, and stronger Sterling, which pushed to a fourteen week high 1.3201, helped by news that the Democratic Unionist Party will support the PMs Brexit deal this week and hopes that exit from the EU will not occur without a deal. Wall Street closed strongly higher, with gains of 0.75-1.3% on the news of the government reopening. Asia/Pacific markets have had a mixed session this morning, as investors remain cautious ahead of earnings reports. The Nikkei turned lower as the Yen firmed but gains were seen in Sydney, lifted by energy and mining stocks.

UK update

According to the CBI Distributive Trades Survey, retail sales volumes were unchanged in the year to this month, following the contraction in December. The outlook for the coming months is more upbeat, with sales volumes and orders expected to increase next month. In December The British Bankers Association reported that mortgages approvals are up by 6.4% from a year earlier. Net mortgage lending rose to £1.325bn, the weakest since August 2016, with credit card lending falling by £0.02bn, the largest fall since April 2016.

Investments

The December MPC meeting delivered the expected no change vote with a unanimous 9-0 vote. The November Inflation Report suggested that inflation could breach the target level within the three year time horizon and later comments that the budget measures had the "potential to be significant" will add to the view that the Bank has its finger on the rate trigger, but has been restrained by the impasse over Brexit. A February/March rate hike is off the table. The markets are still slightly pricing in a hike later in the year, the expectations for November/December rated around 50% likely.

The markets' expectations of a rate cut by the end of this year are seen as about 5% in December, but the possibility has been weakened by a potential of a Brexit delay. Given the volatility of sentiment, and the UK's uncertain Brexit position, the prospect that 2019 may pass without a rate hike remains a possibility

Table 2: Interest rate forecast @ 28-01-19:

	Mar 2019	Jun 2019	Sept 2019	Dec 2019	Mar 2020	Jun 2020	Sept 2020	Dec 2020
Bank rate								
Link	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%
Cap econ	0.75%	1.00%	1.25%	1.50%	1.75%	2.00%	2.00%	2.00%
5yr PWLB rate								
Link	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%
Cap econ	1.90%	2.20%	2.40%	2.70%	2.70%	2.80%	2.80%	2.90%
10yr PWLB rate								
Link	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%
Cap econ	2.30%	2.60%	2.80%	3.10%	3.10%	3.10%	3.10%	3.10%
25yr PWLB rate								
Link	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%
Cap econ	2.80%	3.10%	3.30%	3.60%	3.50%	3.50%	3.40%	3.40%
50yr PWLB rate								
Link	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%
Cap econ	2.70%	2.90%	3.20%	3.20%	3.40%	3.40%	3.40%	3.40%

4. The Council's Capital Expenditure and Financing 2019/20

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 prudential borrowing (internal or external).

The capital expenditure plan is one of the key drivers of the treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

Table 3a: Capital expenditure

	2018/19 Estimated outturn	2019/20 Budget	2020/21 Budget	2021/22 Budget
	£'000	£'000	£'000	£'000
Council's infrastructure capital	81,923	119,200	126,806	82,631
HRA	6,995	13,045	6,154	6,154
Commercial activities	56,602	104,952	17,482	9,951
Total	145,520	237,197	150,442	98,736

Note: The capital strategy forms part of the Council's budget submission which will be presented to full Council in February 2019 and summary by key area can be found in appendix B

The capital financing requirement (CFR) is the total historic outstanding capital expenditure which has not yet been paid for from resources (e.g. capital receipts, capital grants etc.). It is essentially a measure of the Council's indebtedness and its underlying borrowing need to support its capital expenditure plans. Any capital expenditure above which has not immediately been paid for will increase the CFR. Tables 3, 4 and 5 below demonstrate the Council's infrastructure capital, HRA, and Commercial activities CFR.

Table 3b: Capital financing requirement:	**2018/19 Estimated Outturn £'000**	**2019/20 Budget £'000**	**2020/21 Budget £'000**	**2021/22 Budget £'000**
Council's infrastructure capital				
Opening balance (estimated)	**182,899**	**162,289**	**200,023**	**248,413**
Capital expenditure funded by Borrowing	**69,414**	**41,422**	**52,078**	**22,024**
Transfer to commercial activities CFR	**(87,113)**			
Sub Total	**165,200**	**203,711**	**252,101**	**270,437**
Less Minimum Revenue Provision				
MRP charge	**(2,495)**	**(3,340)**	**(3,340)**	**(3,340)**
PFI principal charge	**(283)**	**(215)**	**(215)**	**(215)**
Swap funding /repayment of forward funding	**(133)**	**(133)**	**(133)**	**(133)**
Loan repayment				**(976)**
Sub Total	**(2,911)**	**(3,688)**	**(3,688)**	**(4,664)**
Closing Balance	**162,289**	**200,023**	**248,413**	**265,773**
Movement	**(20,610)**	**37,734**	**48,390**	**17,360**

The increase in the general fund borrowing requirement is due to a large increase in the capital programme for schemes such as the town centre regeneration, loans to group companies and commercial investments; this will later reduce when capital receipts from scheme asset disposals are received or loans repaid. It has also increased as a result of forward funded schemes (where the Council funds infrastructure in advance of agreed developer contributions, to enable developments to proceed). These will be cleared as the developer contributions are received. The CFR is also reduced each year by the minimum revenue provision (MRP) (see section 4).

Table 4: Capital financing requirement:	2018/19 Estimated Outturn £'000	2019/20 Budget £'000	2020/21 Budget £'000	2021/22 Budget £'000
HRA				
Opening balance (estimated)	88,650	85,552	85,372	81,890
Capital expenditure funded by Borrowing	0	1,808	0	0
Sub Total	88,650	87,360	85,372	81,890
Less Minimum Revenue Provision				
Loan repayment	(3,098)	(1,988)	(3,482)	(4,223)
Sub Total	(3,098)	(1,988)	(3,482)	(4,223)
Closing Balance	85,552	85,372	81,890	77,667
Movement	(3,098)	(180)	(3,482)	(4,223)

The table above shows the Housing Revenue account (HRA). The capital expenditure of £13,045k in 2019/20 is funded by the major repairs reserve, HRA revenue contribution, Right to Buy Receipts and borrowing

Table 5: Capital financing requirement:	2018/19 Estimated Outturn £'000	2019/20 Budget £'000	2020/21 Budget £'000	2021/22 Budget £'000
Commercial activities				
Opening balance (estimated)	0	87,113	182,979	194,145
Capital net expenditure funded by Borrowing	0	95,866	11,166	9,951
Transfer from Council's infrastructure capital CFR	87,113			
Sub Total	87,113	182,979	194,145	204,096
Less Minimum Revenue Provision				
*see note below				
Sub Total	0	0	0	0
Closing Balance	87,113	182,979	194,145	204,096
Movement	87,113	95,866	11,166	9,951

*MRP to reviewed and realigned between capital infrastructure CFR and commercial activities CFR during 2019-20

Due to central Government support falling, part of the Council's financial strategy is also based on diversifying income streams, by growing revenue generating assets through its commercial activities (e.g.: housing companies).

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 both the day-to-day running costs of the Council and also its capital plans.

The treasury team manages the daily cash balances to meet daily cash requirements, but on occasions the Council may have to borrow short-term to meet cash-flow requirements and this is permissible under this strategy.

For its capital expenditure, the Council does not have to 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, and the decision on when to borrow is taken by the chief finance officer.

5. Balance sheet forward projection

The following is a forecast funds available for investment/internal borrowing position at year end. Where the funds available for investments go into deficit, this illustrates the need for further external loans.

Table 6: Wokingham Borough Council -Balance Sheet Projections:

	2018/19 Estimated Outturn £'000	2019/20 Budget £'000	2020/21 Budget £'000	2021/22 Budget £'000
CFR (Year-end position)	334,954	468,375	524,448	547,536
Less other long term liabilities	(8,600)	(8,600)	(8,600)	(8,600)
Expenditure to be funded by borrowing	**326,354**	**459,775**	**515,848**	**538,936**
External Borrowing c/fwd.	(145,256)	(181,908)	(295,170)	(348,182)
Loan Maturities	3,348	2,738	41,988	3,482
New Loans	(40,000)	(116,000)	(95,000)	(30,000)
External borrowing	**(181,908)**	**(295,170)**	**(348,182)**	**(374,700)**
Internal borrowing	(144,446)	(164,605)	(167,666)	(164,236)
External Borrowing	(181,908)	(295,170)	(348,182)	(374,700)
Total borrowing	**(326,354)**	**(459,775)**	**(515,848)**	**(538,936)**
Expenditure to be funded by borrowing	326,354	459,775	515,848	538,936
% of internal borrowing to CFR	**42.04%**	**34.51%**	**31.45%**	**29.53%**
Internal borrowing funded by				
General Fund Balance	9,124	9,124	9,124	9,124
Housing Revenue Account Balance (Inc. MRA)	7,511	7,511	7,511	7,511
Collection Fund Adjustment Account	9,338	9,338	9,338	9,338
Earmarked reserve	51,200	51,200	51,200	51,200
Capital Receipts Reserve	5,567	5,567	5,567	5,567
Provisions (exc. any accumulating absences)	3,005	3,005	3,005	3,005
Capital Grants Unapplied	26,397	26,397	26,397	26,397
Reserves available for Investment	**112,142**	**112,142**	**112,142**	**112,142**
Working Capital (Deficit) / Surplus	66,222	66,222	66,222	66,222
Internal borrowing	(144,446)	(164,605)	(167,666)	(164,236)

***Total amount available for investment/ (external borrowing required)**	**33,918**	**13,759**	**10,698**	**14,128**

Total borrowing broken down into CFR Categories				
Council's infrastructure capital	**162,289**	**200,024**	**248,413**	**265,773**
Housing Revenue Account (HRA)	**85,552**	**85,372**	**81,890**	**77,667**
Commercial activities	**87,113**	**182,979**	**194,145**	**204,096**
Less other long term liabilities	**(8,600)**	**(8,600)**	**(8,600)**	**(8,600)**
Total	**326,354**	**459,775**	**515,848**	**538,936**

Total borrowing	**326,354**	**459,775**	**515,848**	**538,936**

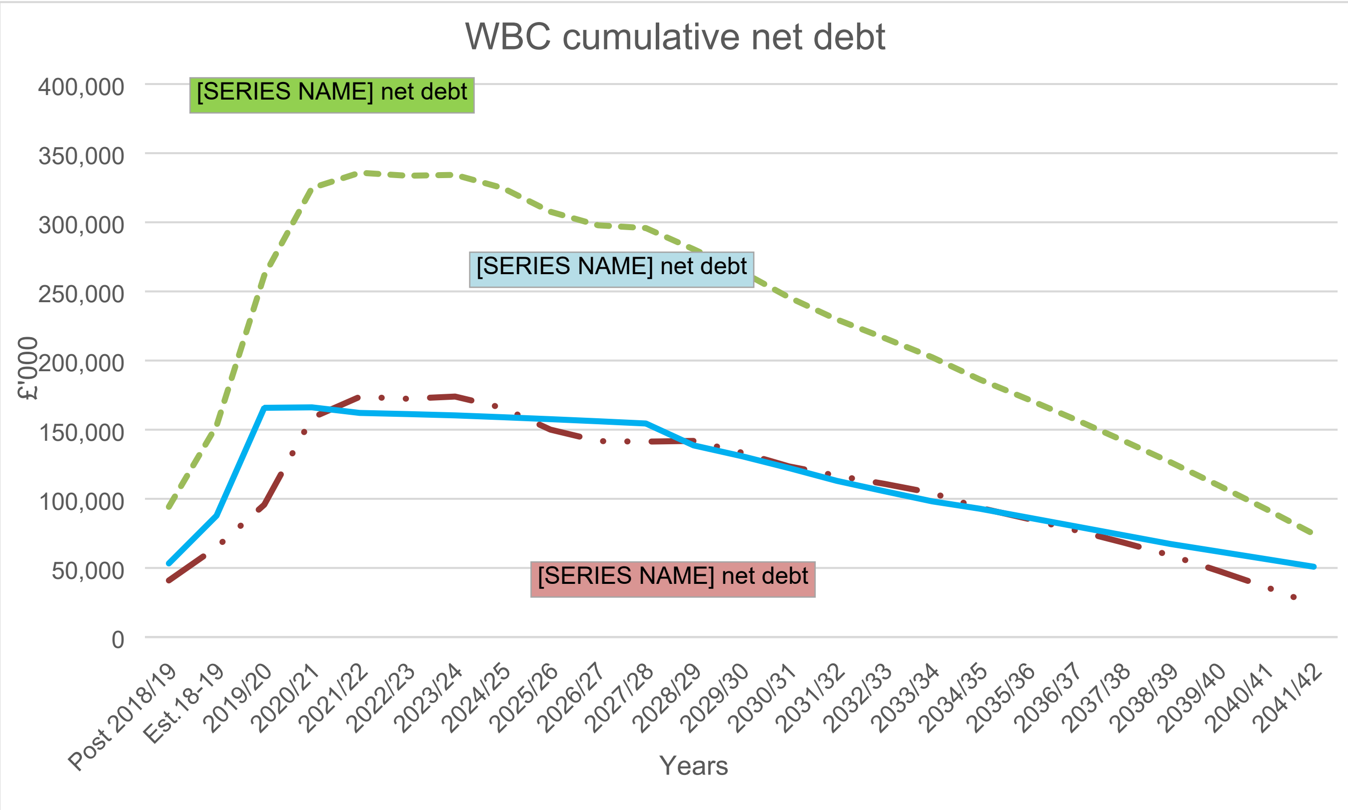
NB*: a targeted sustainable surplus balance of £10m is considered prudent

Total forecast additional borrowing (£539m - £327m = £212m)

The additional borrowing of £212m taken out between 1st April 2019 and 31st March 2022 will be a mixture of external and internal. This is planned to be repaid within 20 years by the following resources:

- Returns on investments from WTCR and WHL including capital receipts
- Returns on investments from Commercial properties
- Developer contributions from forward funded programmes

The graph below illustrates the additional borrowing cumulative net debt over the next 20 years.



The council's capital programme now includes many large infrastructure schemes that span a number of years. It is not uncommon or unreasonable for the profiling of these to be further refined once the initial budget has been approved and the precise timing of expenditure becomes clearer as projects move from feasibility and planning through to delivery.

Our capital finance specialists meet regularly with our key project and programme managers to update predictions and find ways to improve the accuracy of our capital monitoring. This has included the receipt of more detailed information on projects and a new profiling methodology for the capital programme in accordance with The Royal Institute of British Architects (RIBA) planned stage process. Work will continue to do what we can to improve the financial arrangements, however it should be recognised that it contains by its nature, sizeable and often uncontrollable, fluctuations which can often impact on the level of debt financing costs and investment returns in-year.

6. Minimum revenue provision (MRP) policy statement

The Council is required to pay off an element of the accumulated General Fund capital spend each year (the 'CFR') through a revenue charge known as the minimum revenue provision (MRP). The Council is also permitted to undertake additional voluntary payments known as voluntary revenue provision (VRP).

The Ministry for Housing, Communities and Local Government (MHCLG) regulations have been issued which require the full Council to approve a MRP Statement in advance of each financial year. The decision lies with the Council although a prudent provision must be made. The Council is recommended to approve the MRP Statement which can be found in Appendix G.

Some principles in the guidance have been reflected in the Council strategy now the guidance has been finalised. However where we identify an alternative prudent and more pertinent MRP policy, we are permitted to follow that instead.

For 2019/20 Wokingham Borough Council's MRP policy will follow the main MHCLG principles, except in some instances, the table below summarises other area where WBC are planning to divert from the draft guidance.

Table 7: Changes to MRP Guidance

Expenditure type	Guidance maximum 'C', (MRP repayment period)	WBC MRP charging policy
Freehold land	maximum of 50 years	Maximum 60 years
bridges	maximum of 50 years	Maximum 60 years
Investment assets	maximum of 50 years	10% of maximum 60 years asset life
loan capital in WBC holdings	20 years	No charge - Loan covered by Asset
Forward funding Schemes	maximum of 50 years	No charge – Developer contribution are used to repay principle

Under section 21(1A) of the Local Government Act 2003 local authorities are required to "have regard" to this guidance.

The guidance remains guidance not an enforced treatment.

7. External borrowing and compliance with treasury limits and Prudential Indicators for debt

The previous sections cover the overall capital programme but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators found in table 4. Further detail on each of these indicators is included in Appendix D.

Table 8: Prudential Indicator – Debt

	2018/19 Estimated Outturn £'000	2019/20 Budget £'000	2021/22 Budget £'000	2021/22 Budget £'000
Authorised limit £,000	334,954	585,500	656,000	684,500
Gross external borrowing £,000	(181,908)	(295,170)	(348,182)	(374,700)
HRA debt limit £,000	102,000	102,000	102,000	102,000
% of internal borrowing to CFR	42.04%	34.51%	31.45%	29.53%
Maturity structure of borrowing	See Appendix C			
Operational boundary for external debt £'000	334,954	492,000	551,000	575,000
Ratio of financing costs to net revenue stream*	2.55%	3.59%	5.38%	5.79%

*Note: The increase is due to the estimated increase in borrowing for the capital programme but as shown above the savings from this investment are already being shown. (These figures are estimates and will be updated once the MTFP has been approved by budget)

The borrowing requirement above is based on the estimates of capital expenditure in the Council's capital programme and represents the maximum if the programme proceeds as planned. These estimates have been subject to a robust challenge process as the capital programme has been developed. Historical evidence suggests that the programme could be subject to re-profiling between years of up to 50% of the programme on average which means that the figure for borrowing in 2019/20 could be closer to £150 million. This is not a reduction in the overall planned borrowing, but just a deferment to match any capital re-profiling.

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.

8. Investments

The treasury management team ensure the cash flow is adequately planned, with surplus monies being invested in suitable 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.

8.1 Annual investment strategy

CIPFA Code and the MHCLG Guidance require the Council 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 Council's investment priorities will be security first, liquidity second, then return.

The Council may invest its surplus funds in accordance with its time and monetary limits for institutions on the Council's counterparty list, as shown below

	* Minimum credit criteria / colour band*	Money Limit	Max. maturity period
DMADF – UK Government	UK sovereign rating	£20M	3 months
UK Government gilts	UK sovereign rating	£5m	1 year
UK Government Treasury bills	UK sovereign rating	£5m	1 year
Money market funds	AAA	£5m	Liquid
Local authorities	N/A	£5m	2 year
Term deposits with banks and building societies**	AA	£5m	Liquid
Term deposits with building societies	A-	£5m	Liquid
CDs or corporate bonds with banks and building societies	AA	£5m	Liquid

Note*: The credit criteria shown here is Fitch credit ratings agencies long term, When using the credit rating the Council will use the lower of the three credit rating agencies.(See appendix D)

Note **for each banking group the following limits will apply, dependent on the rating of the Parent Bank (i.e. Lloyds group)

- AAA : £7m with a maximum average duration of 1 year
- AA- :£5m with a maximum average duration of 6 months

The investment policies can be found in Appendix D

8.2 Investment projections treasury and non-treasury

The table below shows the Councils investment projections

Table 9: Investments

	2018/19 Estimate £'000	2019/20 Budget £'000	2020/21 Budget £'000	2021/22 Budget £'000
Loans to WHL/HRA/WTCR balance @ 31-03-19	79,032	115,159	123,205	128,887
Rate of return (average)	3.2%	2.8%	2.7%	2.7%
Returns on investment	(2,515)	(3,182)	(3,357)	(3,532)
Local Authorities/fund managers balance @ 31/03/19	83,512	70,770	49,539	34,677
Rate of return (average)	0.5%	0.8%	1.0%	1.2%
Returns on investment	(546)	(531)	(495)	(399)

Interest rates on historic loans to WHL/HRA/WTCR (commercial activities) have been reviewed and updated to reflect current market conditions this has resulted in a small reduction in the average rate of return on historic loans

8.3 Non-Treasury Investments

Although not classed as treasury management activities and therefore not covered by the CIPFA Code or the MHCLG Guidance, the Council may also make loans and investments for service purposes or where the local authority is setting up local authority owned companies. Such loans and investments will be subject to the Council's normal approval processes for revenue and capital expenditure and need not comply with this Treasury Management Strategy. Commercial properties investment will be made in line with previously strategy agreed by Council on 23/11/2017. Where these investments have treasury or MRP implications this strategy will be followed.

8.4 Cash flow management

The Council's officers maintain a detailed cash flow forecast for each coming year revising it as more information is available. This informs the short term investments such as those to cover precept payments. The forecast is compiled on a prudent basis to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Long term investment strategy is based on the Council's medium term financial strategy.

8.4 Estimated Investment return rates

Investment returns are likely to remain low during 2019/20 but to be on a gently rising trend over the next few years'. Political uncertainty will continue to weigh on the economy and imported inflation is likely to be a feature for some time.

8.5 Compliance with treasury limits and prudential indicators for investments

As with debt, the Council has a framework prudential indicators for investment which it is uses to assess its investment strategy. The Council is asked to approve the following indicators found in table 7. Further detail on each of these indicators is included in Appendix D.

Table 8: Prudential Indicator – Investment **2019/20**

Review of investment strategy to be undertaken during year	Yes
Investment risk benchmarking	
Security - The Council's maximum security risk benchmark for the current portfolio, when compared to these historic default tables	0.10%
Liquidity – in respect of this area the Council seeks to maintain:	
Bank overdraft	£0.5m
Liquid short term deposits available with a week's notice of at least	£5m
Weighted average life benchmark is expected to be 0.25 years, with a maximum of 0.5 years.	0.5 Years
Investments – internal returns above the 7 day LIBID rate	
Investment Balance as 31st March 2020	£40.m
Returns on investments	£3.6m

9. Flexible use of Capital Receipts

Since December 2015, the government has provided local authorities with the flexibility of utilising capital receipts for qualifying expenditure. This is to enable authorities to fund transformation and cost reduction programmes from capital receipts rather than revenue expenditure.

The guidance recommends that a strategy should be prepared that includes separate disclosure of the individual projects that will be funded or part funded through capital receipts flexibility and that the strategy is approved by full Council. The Council currently does not plan to use this flexibility.

10. Updates to Treasury Management Strategy

The Director of Corporate Services confirms that the treasury team will abide by the strategy set out within this document and will report to the Audit Committee in November 2019 as part of the mid-year report any breaches to limits and prudential indicators.