LANCASHIRE COMBINED FIRE AUTHORITY
RESOURCES COMMITTEE
Meeting to be held on 27 November 2019

TREASURY MANAGEMENT MID-YEAR REPORT 2019/20

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Executive Summary

The report sets out the Authority's borrowing and lending activities during 2019/20. Decisions taken were in accordance with the Treasury Management Strategy and were based on anticipated spending and interest rates prevailing at the time.

Recommendation

The Authority is asked to note and endorse the report and agree the additional MRP contribution of £187k.

Information

In accordance with the CIPFA Treasury Management Code of Practice and to strengthen members' oversight of the Authority's treasury management activities, the Resources Committee receives a treasury management mid-year report and a final outturn report. Reports on treasury activity are discussed on a quarterly basis with Lancashire County Council Treasury Management Team and the Authority's Director of Corporate Services and are used as a basis for this report to the Committee.

Economic Overview

The economic situation continues to be dominated by the uncertainty arising from the unknown impact of the UK's withdrawal from the European Union and the trade dispute between the worlds' two largest economies namely the USA and China. Despite this, the first quarter of 2019 showed relatively strong growth of 0.5% (1.8% year on year). However, it was considered that this was partly due to stockpiling ahead of the expected date for leaving the European Union and was followed by a contraction of 0.2% in the second quarter.

<u>Outlook for Interest Rates</u>
The uncertainty in the economy has influenced the forecast interest rates. The Bank of England has in recent times raised expectations of gradual increases in interest rates and this has been reflected in interest rate forecasts. Recent forecasts though have reduced this expectation. In their May forecast Arlinglose, Lancashire County Council's treasury advisers, were forecasting that the bank rate would see a 0.25% increase in March 2020 and September 2020. However, with the prevailing economic situation they have changed the forecast to reflect no change in the Bank Rate for the foreseeable future. However, there are risks to this forecast which could see rates moving in either direction.

Recent economic data has suggested that weaker economic growth has occurred, and is anticipated to continue, globally. One of the consequences of this together with the political uncertainty has been that Gilt yields have been volatile over the period and they have fallen to historically low levels. For example the 20 year Gilt yield fell from 1.35% to 0.88% from the end of June to the end of September

Forecast for the key rates provided by Arlingclose are shown below:

Period	Bank Rate	3 month money market	12 month money market	20-year Gilt Rate
Q4 2019	0.75	0.75	0.85	0.95
Q1 2020	0.75	0.75	0.85	1.00
Q2 2020	0.75	0.75	0.85	1.05
Q3 2020	0.75	0.75	0.85	1.10
Q4 2020	0.75	0.75	0.85	1.15
Q1 2021	0.75	0.75	0.85	1.15
Q2 2021	0.75	0.75	0.85	1.15
Q3 2021	0.75	0.75	0.85	1.15
Q4 2021	0.75	0.75	0.85	1.15
Q1 2022	0.75	0.75	0.85	1.15
Q2 2022	0.75	0.75	0.85	1.15
Q3 2022	0.75	0.75	0.85	1.15
Q4 2022	0.75	0.75	0.85	1.15

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 are summarised in the Table below:

	Balance 31/3/19
	£m
Capital Finance Requirement	14.374
Less other debt liabilities	(14.177)
Borrowing Requirement	0.197
External borrowing	2.000
Reserves	36.017
Working capital	(2.045)
Available for investment	33.972
Investments	34.646

The table above shows that the Authority has a net borrowing requirement of £197k, which is below its actual borrowing of £2.0m, and reflects the additional voluntary MRP contributions that the Authority has made in order to generate cash to repay loans either on maturity or as an early repayment,. It is proposed that a further voluntary MRP contribution of £187k, in addition to the planned £10k, is made in order to reduce the borrowing requirement to zero, fully providing for existing loan repayment or to offset future loan drawdowns. (It is worth noting that we are not anticipating in year capital expenditure being funded from borrowing, but depending on the agreed 5 year programme currently being developed some borrowing may be required in future years).

In terms of investments it was anticipated that there may be some reduction in the level of reserves held, dependent upon the level of in-year capital expenditure. Given slippage in the programme this looks less likely at the present time.

Borrowing

There has been no new borrowing in the first six months of the financial year. This is consistent with the position that the current borrowing is already above the CFR and that the capital programme does not include any expenditure to be financed from borrowing.

The long term debt outstanding of £2m is from the Public Works Loan Board. The table below show the maturity profile of the Authority's borrowings, along with an interest rate paid.

Loan Amount (£m)	Maturity Date	Interest rate (%)
0.700	June 2037	4.480
0.650	June 2036	4.490
0.650	December 2035	4.490

Consideration is given to the early repayment of the loans. However, these would be subject to an early repayment (premuim) charge. The authority did repay debt in 2017/18 but at the time it was considered that the premuim on these loans was such that it was not financially beneficial to repay the loans. This is still considered to be the case with the estimated premuim charge to repay the three loans being £1.074m.

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 Authority principally invests in a call account provided by Lancashire County Council which pays the base rate. Each working day the balance on the Authority's Current Account is invested in this to ensure that interest is received on surplus balances within an acceptable risk framework. During the period all new investments were placed with the County Council via this arrangement. At 30th September there was a balance of £33.670m invested in LCC while the average for the period was £21.663m.

In addition, in order to increase the rate earned on current balances, the authority have placed fixed investments with other local authorities. To attract a higher rate of interest than is available on the call account these investments will need to be fixed for a longer period of time. During the year the following investments have been in place:

Start Date	End Date	Principal	Rate	Annual Interest	Interest 2019/20
30/6/14	28/6/19	£5,000,000	2.4%	£120,000	£28,932
18/10/18	19/10/20	£5,000,000	1.15%	£57,500	£57,500
19/11/18	18/11/19	£5,000,000	1.00%	£50,000	£31,644
19/12/18	19/06/19	£5,000,000	0.92%	£46,000	£9,956

At 30 September there was £10m fixed term investment in place therefore the total investment held at 30 September is £43.670m.

The overall the rate of interest earned during this period was 0.96% which compares favourably with the benchmark 7 day index which averages 0.69% over the same period.

All investments are made in accordance with the current Treasury Management Strategy and the CIPFA treasury management code of practice.

Prudential Indicators

In order to control and monitor the Authority's treasury management functions, a number of prudential indicators are determined against which performance may be measured. The indicators for 2019/20 were approved by the Authority on 18 February 2019 are shown in the table below alongside the current actual.

	2019/20 PIs	**Actual at 30/9/19**
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	5.000	2.000
Other long-term liabilities	14.600	13.983
Total	19.600	15.983

	2019/20 PIs	**Actual at 30/9/19**
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	3.000	2.000
Other long-term liabilities	14.000	13.983
Total	17.000	15.983
Upper limit for fixed interest rate exposure		
Borrowing	100%	100%
Investments	100%	22.9%
Upper limit for variable rate exposure		
Borrowing	50%	0%
Investments	100%	77.1%
Upper limit for total principal sums invested for over 364 days (per maturity date)	25.000	10.000
Maturity structure of loan debt	**Upper/ Lower Limits**	**Actual %**
Under 12 months	100% / nil	0%
12 months and within 24 months	50% / nil	0%
24 months and within 5 years	50% / nil	0%
5 years and within 10 years	50% / nil	0%
10 years and above	100% / nil	100%

Revenue Budget Implications

The 2019/20 revenue budget for treasury management activity showed that anticipated income exceeded expenditure by £0.252m. Taking into account the activity for the first six months of the year and estimated cash-flow for the remainder of the year the latest forecast is shown below, and is reflected in the financial monitoring report elsewhere on the agenda:

	Budget	Forecast	Variation
	£m	£m	£m
Interest Payable	0.090	0.090	0.000
Minimum Revenue Provision	0.010	0.197	0.187
Interest receivable	(0.352)	(0.331)	0.021
Net budget	(0.252)	(0.044)	0.208

The variation on the MRP reflects the additional contribution proposed whilst interest receivable is slightly below budget as the anticipated increase in the interest rates in the last quarter of the financial year looks unlikely.

Regulatory Updates

A key source for long term borrowing is the PWLB. The PWLB lending is offered at a fixed rate above the gilt yields. For most authorities which qualify for the certainty rate, including the Lancashire Combined Fire Authority, this rate was 0.8% In recent months gilt yields and therefore loan rates have fallen to record low levels and as a result local authority borrowing from the PWLB has risen. In response to this HM Treasury announced on the 9th October that it was increasing the margin above gilts by 1%. Therefore for an authority which qualifies for the certainty rate then the interest rate on any new PWLB loan is 1.8% above the gilt yield rather than 0.8%.

This change does not have an immediate impact for the authority as it is not seeking new loans. However, should the capital financing position change then consideration will have to be given as to whether there are suitable alternatives to PWLB financing.

Financial Implications

Included within report above.

Human Resource Implications

None

Equality and Diversity Implications

None

Business Risk Implications

The Treasury Management strategy is designed to minimise the Authority'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 the Authority 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.

Environmental Impact

None

Local Government (Access to Information) Act 1985
List of Background Papers

Paper	Date	Contact
Treasury Management Strategy 2019/20	February 2019	Keith Mattinson, Director of Corporate Services
Reason for inclusion in Part II, if appropriate:		