SURREY
COUNTY COUNCIL

Audit & Governance Committee
28 August 2020

2019/20 Treasury Management Outturn Report

Purpose of the report:

This report summarises the Council's treasury management activities during 2019/20, as required, to ensure compliance with the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice (the CIPFA Code) which requires the Authority to approve a treasury management annual report after the end of each financial year.

Recommendations:

It is recommended that the Committee note the content of the Treasury Management Outturn Report for 2019/20 and compliance with all Prudential Indicators.

Background:

1. The Authority has adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the Authority to approve Treasury Management half-year and annual outturn reports. This is the annual outturn report for 2019/20.

2. The Authority's Treasury Management Strategy Statement and Prudential Indicators for 2019/20 were approved at the Audit and Governance Committee on 7 February 2019. The investment and borrowing of cash exposes the Council to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Authority's Treasury management Strategy.

3. An economic commentary provided by our expert Treasury Management Advisors, Arlingclose is included in Annex 1

Treasury Management Annual Report 2019/20

Overview

4. On 31 March 2020, the Authority had net borrowing of £643m arising from its revenue and capital income and expenditure, an increase of £8m since 31 March 2019. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), which represents the amount of capital expenditure that is not funded from capital receipts, government grants, third party contributions or revenue.

5. Net borrowing has increased due to a rise in the CFR as new capital expenditure was higher than the financing applied, including minimum revenue provision. This is set out in table 1, below:

Table 1: Balance Sheet Summary

	31/03/19 Balance £m	2019/20 Movement £m	31/03/20 Balance £m
General Fund CFR	1,234	18	1,252
Less PFI Liabilities	(227)	22	(205)
Gross Borrowing Requirement	**1,008**	**39**	**1,047**
Less usable reserves and working capital	(373)	(31)	(404)
Net Borrowing Requirement	**635**	**8**	**643**

Note: Columns do not sum due to rounding

6. The Treasury Strategy for 2019/20, approved by Audit & Governance Committee in February 2019, continued the policy of internal borrowing. This maintains borrowing below its underlying level by using available reserves and working capital to reduce the need for external borrowing. This minimises interest rate risks and keeps interest costs low.

7. The Council also manages cash on behalf of Surrey Police and Crime Commissioner, the balance of which was £17.4m as at 31 March 2020. The Council accounts for this as short term borrowing. The treasury management position as at 31st March 2020 and the year-on-year change in show in table 2 below.

Table 2: Treasury Management Summary

	31/03/19 Balance £m	2019/20 Movement £m	31/03/20 Balance £m
Long-term borrowing	397	39	436*
Short-term borrowing	255	(33)	222
Surrey Police	14	3	17
Total borrowing	**666**	**9**	**675**
Money Market Funds	(31)	(1)	(32)
Net borrowing	**635**	**8**	**643**

*Total long term borrowing is £442m. This includes £5.5m of Local Enterprise Partnership (LEP) loans which are managed outside of the Treasury Management Strategy.

Borrowing Activity

8. At 31 March 2020, the Authority held £675m of borrowing, an increase of £9m on the previous year. The sources of borrowing, interest rates and the year-on-year change in show in table 3 below.

Table 3: Borrowing Position

	31/03/19 Balance £m	2019/20 Net Movement £m	31/03/20 Balance £m	31/03/20 Rate %
Public Works Loan Board (PWLB)	387	39	426	3.83
Banks (fixed-term)	10	0	10	5.00
Local authorities (short-term)	255	(33)	222	0.81
Surrey Police & Crime Commissioner	14	3	17	0.70
Total borrowing	**666**	**9**	**675**	

9. The Authority's primary consideration when borrowing money is to balance low interest charges and cost certainty over the period, while allowing enough flexibility to renegotiate a portion of the debt portfolio based upon changing strategic needs.

10. In keeping with these objectives, new long term borrowing from PWLB totalling £40.0m was undertaken during 2019/20 to provide cost certainty for a small part of the portfolio at attractive interest rates. All other borrowing was undertaken for a period of less than one year to enable the Authority to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. A summary of the new long term borrowing entered into during the year is shown at table 4 below.

Table 4: New long term borrowing during 2019/20

Principal (£m)	Maturity Date	Term	Interest Rate
10.0	16 Sep 2034	15 years	1.29%
10.0	23 Sep 2034	15 years	1.30%
10.0	26 Sep 2034	15 years	1.20%
10.0	08 Oct 2034	15 years	1.09%

Investment Activity

11. The Authority holds invested funds, representing income received in advance of expenditure, plus reserves and balances held which have not been utilised for internal borrowing.

12. Both the CIPFA Code and government 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 unsuitably low investment income.

13. In furtherance of these objectives, and given the continuing risk and low returns from short-term unsecured bank investments, the Authority has kept its cash balances and investments low throughout 2019/20 and invested funds principally in Money Market Funds to ensure liquidity. During the year, the Authority's investment balance ranged between £0.3m and £125m. The year-end investment position and the year-on-year change in show in table 5 below:

Table 5: Investment Position (Treasury Investments)

	31/03/19 Balance £m	2019/20 Net Movement £m	31/03/20 Balance £m	31/03/20 Rate* %
Banks & building societies	0	0	0	0
Government (incl. local authorities)	0	0	0	0
Money Market Funds	31	1	32	0.69
Total Investments	**31**	**1**	**32**	**0.69**

*weighted average rate

14. The weighted average return on all investments the Council received in the year to 31 March 2020 was 0.69%. This compares favourably against the 0.53% average 7-day London Interbank Bid Rate (LIBID) for the same period.

Financial Implications

15. The outturn for interest paid, interest received and the minimum revenue provision are outlined in table 6 below.

Table 6: Revenue Implications of Treasury Management Activity

	Budget £m	Outturn £m	Variance £m
Interest Paid	20.9	18.9	(2.0)
Interest Received	(0.3)	(0.7)	(0.4)
MRP	14.7	13.8	(0.9)

16. The amount of the Authority's revenue budget required to be set aside for the future repayment of external borrowing is known as the Minimum Revenue Provision (MRP). This amount is calculated by reference to the Council's balance sheet as at the end of the previous financial year. The amount required for 2019/20 was £0.9m less than expected when the budget was set. This was due to lower borrowing in the capital programme for 2018/19.

17. The variance of £2.0m on interest payable relates primarily to the Council's continued short term borrowing strategy. This resulted in rates payable below those assumed when setting the 2019/20 budget.

Compliance Report

18. All treasury management activities undertaken during 2019/20 complied fully with the CIPFA Code of Practice and the Authority's approved Treasury Management Strategy. Compliance with specific investment limits, the authorised limit and operational boundary for external debt, is demonstrated in tables 7 & 8 below.

Table 7: Debt Limits

	2019/20 Max £m	31/03/20 Actual £m	2019/20 Operational Boundary £m	2019/20 Authorised Limit £m	Complied
Total			1,108	1,696	
Less: Other long term liabilities (PFI)			(143)	(143)	
Underlying Borrowing	708	673	966	1,553	✓

19. Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not considered a compliance failure. Total debt did not exceed the operational boundary at any point in 2019/20.

Table 8: Investment Limits

	2019/20 Maximum £m	31/03/20 Actual £m	2019/20 Limit £m	Complied
UK Central Government	0	0	Unlimited	✓
Money Market Funds	125	32	125	✓
Any group of pooled funds under the same management	0	0	25	✓
Any group of organisations under the same ownership	0	0	20	✓
Any single organisation, except the UK Central Government	0	0	20	✓
Unsecured investments with Building Societies	0	0	10	✓

Treasury Management Indicators

20. The Authority measures and manages its exposure to treasury management risks using the following indicators.

Security: The Council has adopted a voluntary measure of exposure to credit risk by analysing the investment portfolio against historic default rates to assess the maximum exposure to default. Table 7 below shows that as a result of all of the Council's investments being in AAA rated funds the Council has reduced its exposure to security risk based on historic default rates of funds of this type.

Table 9: Historic default rates

	31/03/20 Amount £000	Historical Experience of default %	Adjustment for Market conditions %	31/03/20 Estimated maximum exposure to default £000
Deposits with Banks and financial institutions	(a)	(b)	(c)	(a) x (c)
Local Authorities	0	0.00%	0.00%	0
AAA Rated Counterparties	32.200	0.04%	0.15%	48
AA Rated Counterparties	0	0.05%	0.18%	0
A Rated Counterparties	0	0.06%	0.22%	0
Other Counterparties	0			0
Total	**32,200**			**48**

Note: The maximum exposure to default is based on a full-year holding. The AAA rated counterparties represent Money Market Funds (MMFs). These are highly liquid and secure with short maturities and therefore actual exposure is minimal.

Liquidity: The Council manages its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments. The Council maintains a bank overdraft of £100,000, utilises overnight access Money Market Funds and accesses short term borrowing to meet cash flow requirements. The Local Authority market provides readily available funds.

Interest Rate Exposures: This indicator is set to limit the Authority's exposure to interest rate risk by assessing the impact of a 1% rise or fall in interest rates. The indicator was set based upon an average short term borrowing portfolio of £195m. Actual average short term debt was £217m, with rates 0.33% higher than achieved in 2018/19. The actual rate variance is therefore within the limit.

Table 10: Interest Rate exposures

	31/03/20 Actual £m	2019/20 Limit £m	Complied
Upper limit on one year revenue impact of a 1% rise in rates	0.72	1.95	✓
Upper limit on one year revenue impact of a 1% fall in rates	N/A	1.95	✓

Maturity Structure of Borrowing: This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing were:

Table 11: Maturity Structure of Borrowing

	31/03/20 Actual	Upper Limit	Lower Limit	Complied
Under 12 months	35%	50%	0%	✓
12 months and within 24 months	0%	50%	0%	✓
24 months and within 5 years	3%	50%	0%	✓
5 years and within 10 years	2%	75%	0%	✓
10 years and above	60%	100%	25%	✓

Principal Sums Invested for Periods Longer than a year: The purpose of this indicator is to control the Authority's exposure to the risk of interest rate changes.

Table 12: Sums invested for more than one year

	2019/20 Maximum £m	31/03/20 Actual £m	2019/20 Limit £m	Complied
Sums invested for longer than one year	0	0	40	✓

Other Non-Treasury Holdings and Activity

21. Although not classed as treasury management activities, the CIPFA Code requires the Authority to report on investments for policy reasons outside of normal treasury management. This includes service investments for operational and/or regeneration as well as commercial investments which are made mainly for financial reasons.

22. The Authority holds the following non-treasury investments:
    - £142m of directly owned investment property
    - £234m of loans to Halsey Garton Ltd
    - £93m of equity investments in Halsey Garton Ltd
    - £2m of loans to other subsidiaries

23. Such loans and investments have been approved in accordance with the Council's agreed processes. A register of such investments is maintained and performance information is reported to the Strategic Investment Board or the Shareholder and Investment Panel, in accordance with their Terms of Reference.

24. These non-treasury investments generated £7.2m of investment income for the Authority after taking account of direct costs and interest payable.

Implications:

Financial

25. The financial implications of this report are discussed in paragraph 16-17 and were included in the outturn report to Cabinet on 26 May 2020.

Equalities and Diversity Implications

26. There are no direct equities implications of this report

Risk Management Implications

27. The risk management arrangements in relation to treasury management are discussed in paragraph 20.

Next steps:

i. The treasury team will continue to monitor the UK and overseas banking sector and will continue to update this Committee as appropriate

ii. In line with the requirements the CIPFA Code, this Committee will receive a half yearly report on the Council's treasury management activities in December 2020 and a full year report for 2020/21 in July 2021.

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Sources/background papers:
Capital Budget, Prudential Indicators & Treasury Management Strategy 2019/20
CIPFA Code of Practice for Treasury Management
CIPFA Prudential Code

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