

**Report of Chief Officer Financial Services**

**Report to Executive Board**

**Date: 27<sup>st</sup> June 2018**

**Subject: TREASURY MANAGEMENT OUTTURN REPORT 2017/18**

Are specific electoral Wards affected? If relevant, name(s) of Ward(s):	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Are there implications for equality and diversity and cohesion and integration?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Is the decision eligible for Call-In?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Does the report contain confidential or exempt information? If relevant, Access to Information Procedure Rule number: Appendix number:	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No

**Summary of main issues**

1. This report sets out for Members' approval the Treasury Management Outturn Report for 2017/18.
2. This report shows that net external debt at 31<sup>st</sup> March 2017 was £1,954m, £31m higher than the February 2018 forecast. This movement is due to lower than anticipated revenue balances of £38m and a decrease in the borrowing required for the capital programme of £7m. The level of debt and liabilities should be viewed in the context of the Council's assets which were valued at £5.4bn as at 31<sup>st</sup> March 2017.
3. The level of debt has remained within the authorised limit and operational boundary as approved by the Council in February 2018.
4. Net debt savings of £1,514k have been generated against the original budget. These savings are principally due to continuing to fund short term borrowing at low short term rates. Additional movements were the recognition of compounded interest relating to Kirkstall Forge scheme together with a larger than anticipated capitalisation of interest for schemes under construction at the year-end.
5. The average rate of interest paid on the Council's external debt was 3.32% for 2017/18 compared to 3.48% for 2016/17.

**Recommendations**

6. Executive Board are asked to note the Treasury Management outturn position for 2017/18 and that treasury activity has remained within the Treasury Management Strategy and policy framework.

## 1 Purpose of this report

- 1.1 This report provides members with a final update on Treasury Management Strategy and operations in 2017/18.

## 2 Background information

- 2.1 The operation of the treasury management function is governed by provisions set out under part 1 of the Local Government Act 2003, whereby the Council is required to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities (amended 2009 and 2011) in particular:

- The amended 2017 Prudential Code requires that full Council set certain limits on the level and type of borrowing before the start of the financial year together with a number of prudential indicators.
- Any in year revision of these limits must be agreed by Council.
- Policy statements are prepared for approval by the Council at least twice a year.

These codes have been updated and re-issued late in 2017/18 together with the Ministry of Housing, Communities and Local Government (MHCLG) guidance in relation to Investments and Minimum Revenue Provision (MRP). In line with guidance issued these CIPFA codes and MHCLG guidance will be formerly adopted before the end of March 2019.

## 3 Main Issues

### 3.1 Review of Strategy 2017/18

- 3.1.1 Table 1, below shows that net borrowing in 2017/18 was £1,954m, £31m higher than the February 2018 forecast. This movement is due to lower than anticipated revenue balances of £38m and a decrease in the borrowing required for the capital programme of £7m.

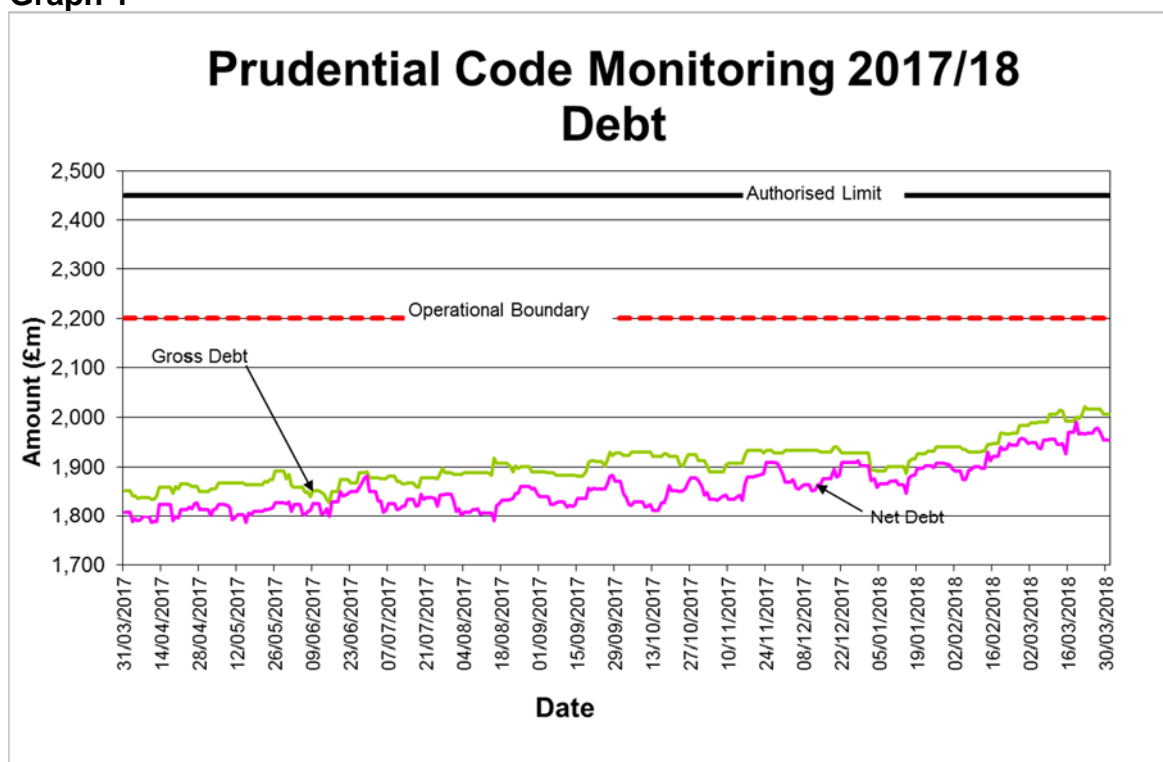
**TABLE 1**

	<b>2017/18 Nov 17 Report</b>	<b>2017/18 Feb 18 Report</b>	<b>2017/18 This Report</b>
<b>ANALYSIS OF BORROWING 2017/18</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
<b>Net Borrowing at 1 April</b>	1,809	1,809	<b>1,809</b>
New Borrowing for the Capital Programme – GF	157	132	<b>123</b>
New Borrowing for the Capital Programme – HRA	0	0	<b>0</b>
Debt redemption costs charged to Revenue (Incl HRA)	(12)	(13)	<b>(11)</b>
Reduced/(Increased) level of Revenue Balances	(5)	(5)	<b>33</b>
<b>Net Borrowing at 31 March</b>	<b>1,949</b>	<b>1,923</b>	<b>1,954</b>
<b>Capital Financing Requirement*</b>			<b>2,198</b>
<b>Other long term liabilities capital financing requirement</b>			<b>612</b>
Net Borrowing 31st March comprised as follows			
Long term Fixed	1,565	1,565	1,595
Variable (less than 1 Year)	0	0	0
New Borrowing	140	114	145
Short term Borrowing	252	264	267
Total External Borrowing	1,957	1,943	2,007
Less Investments	8	20	53
<b>Net External Borrowing</b>	<b>1,949</b>	<b>1,923</b>	<b>1,954</b>
% borrowing funded by short term and variable rate loans	20%	19%	21%
Limit for variable rate Borrowing	40%	40%	40%

\* The Capital Financing Requirement (CFR) is the maximum level of debt (i.e. borrowing and finance leasing) that the Council can hold for its current year capital purposes. The Council is also allowed to borrow in advance for up to two future years capital programmes.

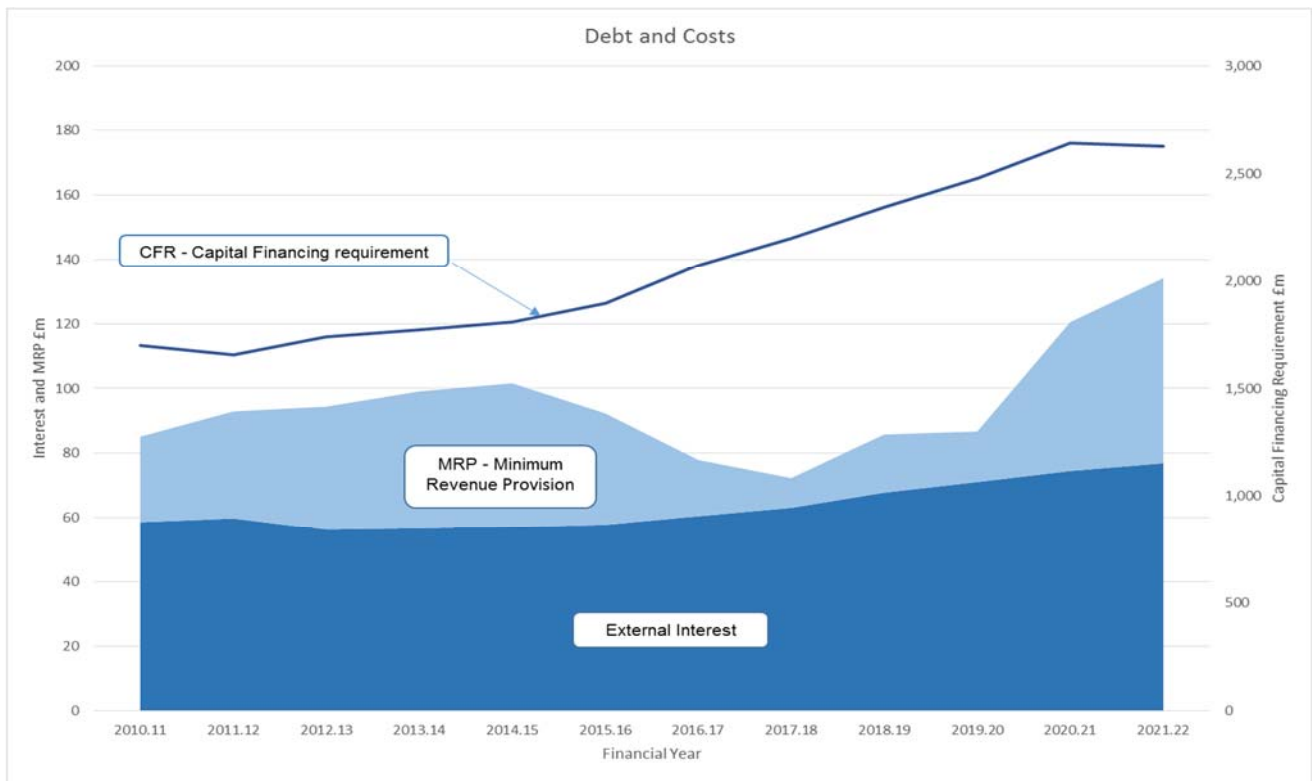
- 3.1.2 The level of debt and liabilities should be viewed in the context of the Council's assets which are valued at approximately £5.4bn as at 31st March 2017. The Capital programme outturn position is reported in the June Financial Performance - Outturn Report to Executive Board elsewhere on the agenda.
- 3.1.3 Graph 1, below shows that the level of debt during 2017/18 remained within authorised limits during the year. The Authorised Limit is the maximum permitted amount of borrowing the Council can have outstanding at any given time and has not been breached during 2017/18. The operational boundary is a key management tool and can be breached temporarily depending on cash flow. This limit acts as a warning mechanism to prevent the authorised limit from being breached. Treasury management activity has resulted in no breach of its prudential indicators which are detailed in Appendix A. All of these other prudential indicators are within normal tolerance levels of treasury management.

**Graph 1**



- 3.1.4 The 2017/18 borrowing strategy continued to fund the capital programme borrowing requirement from short dated loans and internal cash balances whilst looking for opportunities to lock into attractive longer dated funding. Whilst this approach continues to deliver lower costs of financing, the proportion of borrowing funding by short terms loans has reached 20% (Table1). This exposure to interest rate refinancing has increased and is expected to keep on rising to 32% in 2020/21.
- 3.1.5 Graph 2 shows the projected path of the Councils debt and debt financing costs

Graph 2



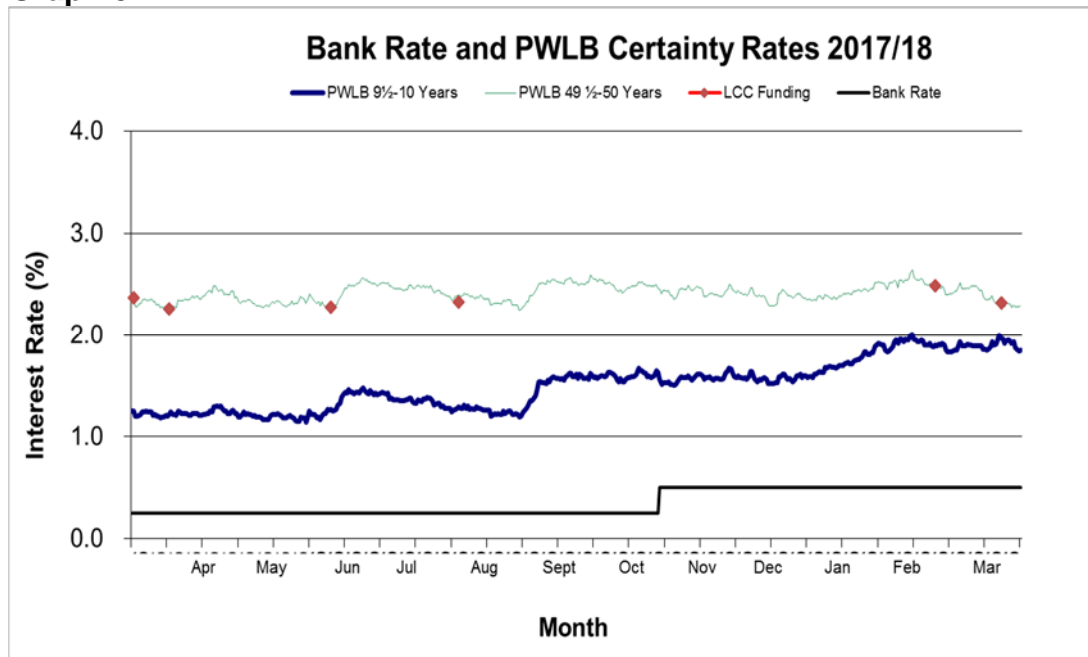
3.1.6 The Capital and treasury reports to Executive Board in February 2018 outlined that the Council was seeking to deliver capital investment of £1,129.0m for the 3 year period starting from 2018/19. This includes committing £458.4m of its own funding to deliver the Council’s priorities and objectives. The council’s borrowing will include £143.3m of capital expenditure that is funded by additional income, generates revenue savings or ensures that our assets are maintained to an acceptable standard. Over the same period the Council is also reducing its borrowing by making debt repayments of £91m. On the basis of the current approved capital programme graph 2 shows the projected increase in the Council’s debt as represented by its CFR and also the projected increase in cost of funding it, reflecting assumptions as to higher interest rates in the future and the unwinding of MRP savings that are exhausted in 2019/20. Monitoring of debt costs will be reported back to Executive Board in the monthly budget monitoring reports and the treasury half year update report. In addition the medium term financial strategy will consider the affordability of the capital programme in the context of increased capital expenditure, borrowing and MRP costs.

- 3.1.7 Since the economic update to Members in February, the economy has continued to expand however inflation remains above the 2.0% target set by the Monetary Policy Committee (MPC) and currently stands at 2.4%. The key movements are:
- Inflation as measured by the CPI index has steadily increased over the year to 3.1% in November before falling back to 2.5% in March and 2.4% in April mainly driven by the fall in value of sterling post the EU referendum. Some commentators believe further falls in inflation may face headwinds however the economy has started 2018 slowly.
  - Average earnings however remain a key indicator of domestic inflation and have increased with the 3 months to March showing 2.6% annualised but was below CPI inflation for much of the year. This represents a reduction in household disposable income with service sector growth consequently being weak.

- UK growth did pick up in the second half of the year resulting in a base rate rise in November 2017 effectively withdrawing the emergency rate cut following the EU referendum in 2016. This subsequent pickup brought forward expectation of an earlier base rate rise however this failed to materialise at the May MPC meeting as mixed data on the UK economy emerged.
- Unemployment continues to fall with the rate over the same period being 4.20% in comparison to the 4.60% a year earlier.
- The US economy grew at an average of 2.3% on average in 2017. The US was the first western economy to begin the process of rate normalisation with the Federal Open Markets Committee (FOMC) increasing rates from December 2015 to a current range of 1.50% to 1.75% with more rises expected in 2018. Unemployment has fallen to 4.1% however inflationary pressures are building in part through the recent tax cuts. The US is also the first to begin unwinding its QE programme by not re-investing maturing debt.
- In Europe growth of 2.3% was achieved however inflation remains stubbornly below the 2% target at 1.4% and this despite continuing injections of Quantitative Easing (QE) in the form of bond and commercial paper purchases.
- In China the problems of excess industrial capacity, stock of un-sold property and non-performing loans in the bank and credit systems remain.
- GDP growth in Japan has improved to 2.1% however inflation again remains below target at 1.5% despite continued monetary and fiscal stimulus.
- Oil prices have climbed steadily during the year from around \$50 per barrel to around \$75-\$80 currently. As fuel costs have a significant impact on many areas of the economy this is likely to support higher level of inflation.
- The Councils treasury management advisors, Link Asset Services are currently forecasting Q4 2018 for the next rise from its current 0.5%. This will of course be dependent on economic performance both here and abroad over the near to medium term and is being kept under review.

3.1.8 Graph 3 below shows the movement in PWLB interest rates over the year. Gilt yields have largely remained range bound at the longer maturity dates and PWLB rates have mirrored this trend. Longer term (49½-50 year) have varied during the year and ended the year at lower levels than the start but not at the low point which occurred in September. Shorter term rates (9½-10 year) have risen from the start of the year and finished higher but in this time frame the low point occurred in June. Commentators following the lead of the Bank of England are expecting a series of steady increases over the next few years and the first rise did occur in November back to 0.50% which reversed the cut after the Brexit vote in 2016. The graph below also shows the long term funding activity undertaken as detailed in table 2 below.

**Graph 3**



3.1.9 Net debt savings of £1,514k have been generated against the original budget. These savings are principally due to continuing to fund short term borrowing at low short term rates. Additional movements were the recognition of compounded interest relating to Kirkstall Forge scheme together with a larger than anticipated capitalisation of interest for schemes under construction at the year-end.

3.1.10 Table 2 shows £125m of longer term funding was secured during the year. The table also shows that no market loans options were exercised during the entire year, no loans either PWLB or market reached maturity during the period. Approximately half of market loans outstanding are termed Lenders Option Borrowers Option (LOBO) and contain clauses which allows the lender, at pre-determined dates, to vary the interest rate on the loan. If one of these options is exercised and the new rate is not accepted, the borrower then has the option to repay the loan without penalty. Members should note that the 2016/17 Council Statement of Accounts have been challenged on the use of LOBOs and are yet to be signed off by the Council's external auditors. Further updates will be provided through the year in following treasury management reports, revenue budget updates and to Corporate Governance and Audit Committee.

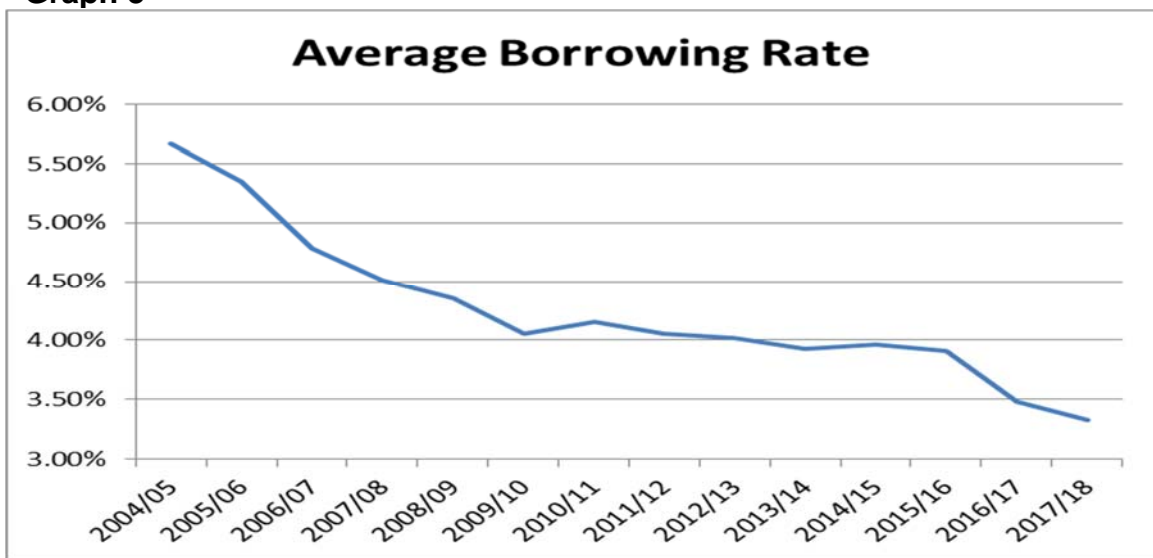
**Table 2**

Loan repayments and borrowing 2017/18							
Loan Repayments				New Borrowing			
Date	Amount	Original Rate	Discount Rate	Date	Amount	Term	Interest Rate
	(£m)	(%)			(£m)	(Years)	(%)
PWLB Loans				PWLB			
				03/04/2017	20.000	50	2.37
				19/04/2017	20.000	47	2.26
				26/06/2017	20.000	50	2.28
				15/08/2017	35.000	49	2.33
				26/02/2018	10.000	50	2.49
				22/03/2018	20.000	50	2.32
<b>Sub Total</b>	<b>0</b>				<b>125.000</b>		
Non PWLB Loans (Call date)				Non PWLB Loans			
<b>Sub Total</b>	<b>0</b>				<b>0</b>		
<b>Total</b>	<b>0</b>			<b>Total</b>	<b>125.000</b>		

**3.2 Interest Rate Performance and Average Maturity Profile**

3.2.1 The average rate of interest paid on the Council’s external debt was 3.32% (down from 3.48%) as shown in Graph 3. This fall is due to the increasing level of the Council debt, both long and short term, which is being funded at historically low levels.

**Graph 3**



3.2.2 Whilst the average borrowing rate remains low it is important to note the average maturity profile of the Council’s debt. The average length of all loans to final maturity including temporary loans is 30.5 years. The average length of all loans to the next option date including temporary loans is 25.0 years. This provides a large degree of funding certainty within the overall debt portfolio. Appendix B analyses debt as at 31<sup>st</sup> March 2018 by interest rate band and the year of maturity or first option date for LOBO loans. The final maturity of LOBO loans is shown as a memo item in the table at the bottom of Appendix B.

## **4 Corporate Considerations**

### **4.1 Consultation and Engagement**

- 4.1.1 This report is an update on strategy as presented to Executive Board in February, as such no consultation has taken place. However, consultation with the Council's treasury advisors takes place regularly throughout the year.
- 4.1.2 The borrowing requirement is an outcome of the capital programme which has been the subject of consultation and engagement as outlined in the February capital programme report.

### **4.2 Equality and Diversity / Cohesion and Integration**

- 4.2.1 Equality, diversity, cohesion and integration requirements are addressed as part of individual capital scheme and programme approvals. The borrowing to deliver these capital schemes is executed through treasury strategy and as such there are no further equality, diversity, cohesion and integration issues.

### **4.3 Council Policies and Best Council Plan**

- 4.3.1 Treasury management strategy secures funding for the council's capital programme that supports the authority's policies and priorities as set out in the Best Council Plan. These include our Best Council ambition to be an efficient and enterprising organisation.

### **4.4 Resources and Value for Money**

- 4.4.1 This update on the treasury strategy recognises the borrowing necessary to fund the capital programme requirements of both General Fund and HRA. The revenue costs of borrowing are included within the revenue budgets of the General Fund and HRA.
- 4.4.2 Net debt savings of £1,514k against the budget have been delivered.

### **4.5 Legal Implications, Access to Information and Call In**

- 4.5.1 In accordance with the Council's Budget and Policy Framework, decisions on borrowing limits, treasury management indicators, investment limits and the Treasury management Policy Statement are approved by Council. Monitoring reports are considered by Executive Board and are subject to call in. There are no further legal, access to information or call in issues.

### **4.6 Risk Management**

- 4.6.1 This report sets out performance against the 2017/18 treasury strategy. The execution of strategy and associated risks are kept under regular review through:
- Monthly monitoring of debt costs and reporting forms part of the monthly update on the Council's Revenue position to Executive Board.
  - Quarterly strategy meetings with the Director of Resources and the Council's treasury advisors.
  - Regular market, economic and financial instrument updates and access to real time market information.



## **5 Conclusions**

- 5.1 This Treasury Management Outturn Report for 2017/18 provides a final update on loans undertaken to fund the capital programme requirements for both General Fund and HRA. Treasury activity during the year was conducted within the approved borrowing limits for the year and resulted in overall savings to the revenue budget as detailed in 3.1.9.

## **6 Recommendations**

- 6.1 Executive Board are asked to note the Treasury Management outturn position for 2017/18 and that treasury activity has remained within the treasury management strategy and policy framework.

## **7 Background documents <sup>1</sup>**

None

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<sup>1</sup> The background documents listed in this section are available for download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.

## Leeds City Council - Prudential Indicators 2017/18

No.	PRUDENTIAL INDICATOR	Feb 17 Report	Feb 18 Report	Outturn (This Report)
<b>(1). EXTRACT FROM BUDGET AND RENT SETTING REPORTS</b>				
<b>Ratio of Financing Costs to Net Revenue Stream</b>				
1	General Fund - Excluding DSG	10.19%	9.94%	9.31%
2	HRA	11.28%	11.31%	11.26%
<b>Impact of Unsupported Borrowing on Council Tax &amp; Housing Rents</b>				
		<b>£ . P</b>	<b>£ . P</b>	<b>£ . P</b>
3	increase in council tax B7 (band D, per annum) (Note 1)	50.72	9.11	8.40
4	increase in housing rent per week	0.08	-	-
5	<b>Net Borrowing and the capital financing requirement (Note 2)</b> The Net borrowing Requirement should not exceed the CFR	OK	OK	OK
<b>Estimate of total capital expenditure (including PFI)</b>				
		<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
6	General Fund	259,154	258,965	230,400
7	HRA	120,645	84,292	85,803
TOTAL		379,799	343,257	316,203
<b>Capital Financing Requirement (as at 31 March)</b>				
		<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
8	General Fund	1,996,815	2,004,600	2,004,600
9	HRA	829,962	815,075	815,075
TOTAL		2,826,777	2,819,675	2,819,675
9a	<b>Limit on HRA Indebtedness as implemented under self financing</b>	721,327	721,327	721,327

No.	PRUDENTIAL INDICATOR	Feb 17 Report	Feb 18 Report	Outturn (This Report)
<b>(2). TREASURY MANAGEMENT PRUDENTIAL INDICATORS</b>				
		<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
10	<b>Authorised limit for external debt - (Note 3)</b>			
borrowing		2,450,000	2,450,000	2,450,000
other long term liabilities		740,000	740,000	740,000
TOTAL		3,190,000	3,190,000	3,190,000
11	<b>Operational boundary - (Note 3)</b>			
borrowing		2,200,000	2,200,000	2,200,000
other long term liabilities		720,000	720,000	720,000
TOTAL		2,920,000	2,920,000	2,920,000
14	<b>Upper limit for fixed interest rate exposure</b> expressed as either:- Net principal re fixed rate borrowing / investments OR:-	115%	115%	115%
15	<b>Upper limit for variable rate exposure</b> expressed as either:- Net principal re variable rate borrowing / investments OR:-	40%	40%	40%
		<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
17	<b>Upper limit for total principal sums invested for over 364 days</b> (per maturity date)	150,000	150,000	150,000
18	<b>Net Debt as a Percentage of gross Debt</b>	99.61%	98.97%	97.37%

16	Maturity structure of fixed rate borrowing 2017/18	Lower Limit	Upper Limit	Actual 31/03/18	
	under 12 months	0%	15%	3%	
	12 months and within 24 months	0%	20%	5%	
	24 months and within 5 years	0%	35%	11%	
	5 years and within 10 years	0%	40%	5%	
	10 years and within 20 years			2%	
	20 years and within 30 years			0%	
	30 years and within 40 years	25%	90%	40%	76%
	40 years and within 50 years			26%	
	More Than 50 Years			8%	
				100.0%	

## Notes.

- The code requires that the Council identifies the capital financing costs arising from unsupported borrowing expressed as the amount per band D property.
- In order to ensure that over the medium term net borrowing will only be for a capital purpose, the Council should ensure that net external borrowing does not exceed the total capital financing requirement in the preceding year plus estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence.
- Limits are the same as the Feb 18 report.
- Prudential indicator 12 relates to actual external debt at 31st March, which is reported in the main body of this report.

**Debt as at 31st March 2018**

**Appendix B**

Table below shows a breakdown of the maturity structure of the authority giving totals

Year Ending 31st March	to 2%	2% to 2.99%	3% to 3.99%	4% to 4.99%	Greater Than 5%	Principal
<b>Fixed Rate Loans - LOBO to First Option</b>						
2019	10,000	5,000	41,436	50,000	-	106,436
2020	-	-	46,436	35,000	-	81,436
2021	-	-	13,812	55,000	-	68,812
2022	-	-	41,436	15,000	-	56,436
2023	-	20,000	27,624	-	-	47,624
2024	-	-	15,000	26,436	-	41,436
2025	-	-	-	-	-	-
2026	-	-	-	-	-	-
2027	5,675	-	28,812	-	-	34,487
2028	-	-	-	-	-	-
2029	-	-	20,000	-	-	20,000
2034	-	-	-	-	-	-
2035	-	-	5,000	-	-	5,000
2052	-	-	-	28,727	-	28,727
2053	-	-	-	145,396	-	145,396
2054	-	-	-	49,347	-	49,347
2055	-	-	5,000	75,782	-	80,782
2056	-	-	10,000	72,173	-	82,173
2057	-	-	-	115,436	-	115,436
2058	-	-	-	102,218	14,099	116,317
2059	-	-	-	-	-	-
2060	-	-	-	-	-	-
2061	-	-	-	17,624	-	17,624
2062	-	-	17,624	-	-	17,624
2063	-	20,000	-	-	-	20,000
2064	-	40,000	10,000	-	-	50,000
2065	-	40,000	-	-	-	40,000
2066	-	40,000	10,000	35,000	-	85,000
2067	-	55,000	30,000	5,000	-	90,000
2068	-	70,000	-	-	-	70,000
2069	-	-	-	-	-	-
2077	-	-	20,000	-	-	20,000
2078	-	-	-	85,000	-	85,000
2079	-	-	-	20,000	-	20,000
<b>Sub Total</b>	<b>15,675</b>	<b>290,000</b>	<b>342,178</b>	<b>933,137</b>	<b>14,099</b>	<b>1,595,090</b>

<b>Temporary Loans</b>						
2019	411,700	-	-	-	-	411,700
<b>Sub Total</b>	<b>411,700</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>411,700</b>

<b>CABP</b>	<b>427,375</b>	<b>290,000</b>	<b>342,178</b>	<b>933,137</b>	<b>14,099</b>	<b>2,006,790</b>
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<b>Memo : LOBO Variable Rate Loans to Maturity</b>						
2047	-	-	-	-	-	-
2055	-	-	-	15,000	-	15,000
2056	-	-	-	45,000	-	45,000
2066	-	-	10,000	10,000	-	20,000
2067	-	-	25,000	15,000	-	40,000
2077	-	-	40,000	15,000	-	55,000
2078	-	-	-	55,000	-	55,000
2079	-	-	-	-	-	-
<b>Sub Total</b>	<b>-</b>	<b>-</b>	<b>75,000</b>	<b>155,000</b>	<b>-</b>	<b>230,000</b>

LOBO's Shown at Maturity in Bottom Memo Section.

LOBO's included in main section at next option date. (Highlighted)