LONDON BOROUGH OF NEWHAM

COUNCIL

Report title	Treasury Management Strategy Statement (TMSS) 2019/20, Treasury Management Annual Investment Strategy (AIS) 2019/20 and Medium Term Capital Strategy Report	
Date of Meeting	**18th March 2019**	
Lead Officer and contact details	**Alison Mackie** **0203 373 9833** **Alison.mackie@newham.gov.uk**	
Director, Job title	**Treasury Manager**	
Lead Member	**Cllr Terrence Paul, Cabinet Member for Finance and Corporate Services**	
Key Decision?	~~Yes~~ / No	Reasons:
Exempt information & Grounds	~~Yes~~ / No	Grounds:
Wards Affected	All	
Appendices **(if any)**	Appendix 1 Capital Prudential Indicators Appendix 2 Treasury Prudential Indicators Appendix 3 Interest Rate Forecasts Appendix 4 Borrowing in Advance of Need Appendix 5 Minimum Credit Rating Appendix 6 Specified and non specified Appendix 7 Treasury Management Policy Statement Appendix 8 Medium Term Capital Strategy Newham	

1 Executive Summary

1.1 The TMSS and AIS are part of the council's reporting procedures and are recommended by the Chartered Institute of Public Finance and Accountancy (CIPFA) code of practice on treasury management and its prudential code for capital finance in local authorities. The Local Government Act 2003 requires Council's to comply with both codes.

1.2 This council has serious concerns regarding the mis-selling of LOBO loans and manipulation of the LIBOR (London Interbank Offered Rate) rate by Barclays and potentially other banks. Newham was the first of a number of local authorities to issue a High Court claim of misrepresentation in respect of LIBOR manipulation.

2 Recommendations

2.1 Council is asked to note this report.

3 Background

3.1 Revised reporting is required for the 2019/20 reporting cycle due to revisions of the Ministry of Housing communities and Local Government (MHCLG) Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a capital strategy, **Appendix 8**, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011.

3.2 It is a statutory duty for the council to determine and keep under review how much it can afford to borrow.

3.3 The council has signed up to ‘the Code’ which requires that the total capital investment remains with sustainable limits and that the impact upon its future council tax and council rent levels is ‘acceptable’.

3.4 The Council is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals.

a. Prudential and treasury indicators and treasury strategy. The first, and most important report is forward looking and covers:

- the capital plans, (including prudential indicators);
- the treasury management strategy, (how the investments and borrowings are to be organised), including treasury indicators; and
- an investment strategy, (the parameters on how Treasury investments are to be managed).

b. A mid-year treasury management report – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

c. An annual treasury report – This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

3.5 The above reports are required to be adequately scrutinised before being recommended to the Council. The TMSS and AIS 2019/20 was scrutinised by Audit Board 12 February 2019

4 Key Considerations & Proposals

4.1 Treasury Management Strategy for 2019/20

4.1.1 The strategy for 2019/20 covers two main areas:

Capital issues

- the capital expenditure plans and the associated prudential indicators

Appendix 1

Treasury management issues

- the current treasury position; See table 1 below
- treasury indicators which limit the treasury risk and activities of the Council -

Appendix 2

- prospects for interest rates; Appendix 3
- the borrowing strategy;
- policy on borrowing in advance of need; Appendix 4
- debt rescheduling;
- the investment strategy;
- creditworthiness policy;
- the policy on use of external service providers

4.1.2 These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, MHCLG MRP Guidance, the CIPFA Treasury Management Code and MHCLG Investment Guidance.

4.2 Training

4.2.1 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 from CIPFA on treasury management basics has been undertaken by members and further training will be arranged as required.

4.2.2 The training needs of treasury management officers are periodically reviewed.

4.3 Service Delivery and Performance Issues

4.3.1 The Council's capital expenditure plans are the key driver of 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. **Appendix 1**

4.3.2 Current Portfolio Position

4.3.2.1The overall treasury management portfolio as at 31 March 2018 and for the position as at 31 December 2018 are shown below for both borrowing and investments.

Table1: Current Portfolio Position

TREASURY PORTFOLIO	Actual 31/3/18 £000	Actual 31/3/18 %	Current 31/12/18 £000	Current 30/12/18 %
Treasury Investments				
Banks	184,000	33	141,000	27
Building Societies	14,000	3	18,000	3
Local Authorities	327,500	59	372,000	69
Money Market funds	-		-	
Bonds	29,500	5	5,000	1
Total Treasury Investments	555,000	100	536,000	100
Treasury External Borrowing				
Local Authorities	135,000	15	64,600	8
PWLB	208,001	23	207,474	25
Market Fixed Debt	256,500	28	258,500	31
Market LOBO's	315,000	34	315,000	36
Mortgage Debt	2		2	
Total External Borrowing	914,503	100	845,576	100
Net Treasury Investments/Borrowing	359,503		309,576	

4.3.3 The Council's forward projections for borrowing are summarised below in Table 2. The table shows the actual external debt, against the underlying capital borrowing need, (the Capital Financing Requirement - CFR), highlighting any over or under borrowing

Table 2: Capital Financing Requirement (CFR)

£m	2017/18 Actual	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Capital Financing Requirement					
CFR – non housing	796	803	815	842	869
CFR – housing	198	217	257	265	265
CFR - Commercial activities/ non-financial investments	110	150	223	325	428
Total CFR	1,104	1,170	1,295	1,432	1,562
Movement in CFR		66	125	137	130

Movement in CFR represented by					
Net financing need for the year (above)	………	78	138	151	144
Less MRP/VRP and other financing movements	………	(12)	(13)	(14)	(14)
Movement in CFR	………	66	125	137	130

4.3.4 Within the above figures the level of debt relating to commercial activities / non-financial investment is detailed in table 3 below

Table 3: Commercial/Non Financial debt

£m	Actual 2017/18	Estimate 2018/19	Estimate 2019/20	Estimate 2020/21	Estimate 2021/22
External Debt for commercial activities / non-financial investments					
Actual debt at 31 March £m	102	151	233	233	378
Percentage of total external debt %	9	18	25	23	23

4.3.5 Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits – see **Appendix 2**

4.3.6 The Interim Director of Financial Sustainability reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

4.4 Prospects for Interest Rates

4.4.1 Current Forecasts are shown in **Appendix 3**

4.4.2 Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The forecast, (and MPC decisions), will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

4.5 Borrowing Strategy

4.5.1 Caution will be adopted with the 2019/20 treasury operations. The Director of Financial Sustainability will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances.

4.5.2 As short-term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long-term debt to short-term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

4.5.3 The reasons for any rescheduling to take place will include:

* the generation of cash savings and / or discounted cash flow savings;
* helping to fulfil the treasury strategy;
* enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

4.5.4 Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

4.5.5 All rescheduling will be reported to the Cabinet at the earliest meeting following its action.

4.5.6 In October 2018, Prime Minister Theresa May announced a policy change of abolition of the HRA debt cap. The Chancellor announced in the Budget that the applicable date was 29/10/18

4.5.7 This council's policy on borrowing in advance of need can be found at **Appendix 4**

4.6 Annual Treasury Management Investment Strategy

4.6.1 The MHCLG and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy, (a separate report).

4.6.2 The Council's investment policy has regard to the following: -

- MHCLG's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the Code")
- CIPFA Treasury Management Guidance Notes 2018

4.6.3 The Council's investment priorities will be security first, portfolio liquidity second and then yield, (return).

4.6.4 The above guidance from the MHCLG and CIPFA place a high priority on the management of risk. This authority has adopted a prudent approach to managing risk, it's minimum credit criteria is set out in **Appendix 5**

4.6.5 The council will consider placing longer term treasury deals while investment rates are at historically low levels where attractive interest rates with high quality counterparties become available.

4.6.6 Investments will make reference to the core balance, cash flow requirements and the outlook for short and medium term interest rates.

4.6.7 Credit ratings should not be the sole determinant of the quality of an institution, this council is not bound by the agency with the lowest rating and, importantly, officers will continually assess and monitor the financial sector and the economic, /political environment in which institutions operate.

4.6.8 An opportunity to invest in an asset backed pooled fund with social and ethical secured assets (PSSIF) generating competitive market returns is currently being considered. This council will be working alongside other local authority partners in development and due diligence of investments. This category of fund is included in **Appendix 6** for approval by Council.

4.6.8 Treasury investment instruments identified for use in the financial year are listed in **Appendix 6** under the 'specified' and 'non-specified' investment categories.

4.6.9 The Director of Financial Sustainability will, on advice, make operational changes to these limits in response to prevailing market conditions and regulatory changes.

4.6.10 All investments will be denominated in sterling.

4.6.11 The Treasury Management Policy Statement is detailed in **Appendix 7** to this report

4.7 Regulatory changes

4.7.1As a result of the change in accounting standards for 2018/19 under IFRS 9, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund

4.7.2 Following the consultation undertaken by MHCLG, on IFRS9 the Government has introduced a mandatory statutory override for local authorities to reverse out all unrealised fair value movements resulting from pooled investment funds. This will be effective from this financial year, 1 April 2018. The statutory override applies for five years from this date. Local authorities are required to disclose the net impact of the unrealised fair value movements in a separate unusable reserve throughout the duration of the override in order for the Government to keep the override under review and to maintain a form of transparency.

4.7.3 The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), are required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as “ring-fencing”. Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

4.7.4 Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank, (RFB), will be focused on lower risk, day-to-day core transactions, whilst more complex and “riskier” activities are required to be housed in a separate entity, a non-ring-fenced bank, (NRFB). This is intended to ensure that an entity’s core activities are not adversely affected by the acts or omissions of other members of its group.

4.7.5 Whilst the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The Council will continue to assess the new-formed entities in the same way that it does others and those with sufficiently high ratings, (and any other metrics considered); will be considered for investment purposes.

4.7.6 This authority will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year.

4.8 Treasury Indicators

4.8.1 Local benchmarks are: 7 day LIBID rate, Link Asset Services (LAS) rate and the UK Debt Management Office (DMO)

4.8.2 The indicators cover 2017/18-2021/22. The CIPFA Prudential Code and the TM code requires authorities to set treasury indicators and these are set out in Appendix 2. No breaches in the indicators are expected in 2019/20.

4.9 Policy on the use of external service providers

4.9.1 The Council uses Link Asset Services, Treasury Solutions as its external treasury management advisors.

4.9.2 The Council recognises that responsibility for treasury management decisions remains with the organisation at all times. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

5 Alternatives considered

5.1 N/A

6 Consultation

6.1 Name of Lead Member consulted: Position: Cllr Terrence Paul, Cabinet Member for Finance and Corporate Services Date: 12/02/19

6.2 This report was noted by Audit Board 12/02/19

7 Implications

7.1 Financial Implications

7.2 The recommended TMSS and AIS including the Treasury and Capital Prudential indicators will provide sufficient flexibility for the Director of Financial Sustainability to manage the council's loan debt effectively in 2019/20. The capital financing forecast used for the budget strategy is consistent with the proposals in this report

7.3 The proposals in this report do not have a direct economic impact within the borough. Clearly though the effective operation of treasury activities should contribute towards the financial standing of the council and the budget strategy that supports the delivery of objectives generally

7.4 **Legal Implications**

7.4.1 The Treasury Management Annual Report is a requirement of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities. Local Authorities are required by regulation to have regard to both codes when carrying out their duties in England and Wales under Part 1 of the Local Government Act 2003. Paragraph 1 of this report confirms that this report has been produced in accordance with both codes

7.5 **Equalities Implications**

7.5.1 The report has no specific impact on Equalities/Diversity other than the achievement of financial savings that will help to maximise resources available for Council services

7.6 **Other Implications relevant to this report:**

7.6.1 None

8 Background Information used in the preparation of this report

8.1 Statutory requirement to list

CIPFA – Treasury management in the public services – code of practice & guide for chief financial officers
CIPFA Prudential code for local authority capital finance
Sector treasury services Ltd. UK economic forecasts
London Borough of Newham – Treasury management strategy 2017/18 and MRP Policy statement
Treasury management practices
Local Government Act 2003
CLG Guidance on local authority investments 2010
CLG MRP Guidance
CIPFA – Treasury and investment management in UK local authorities – Guidance notes for practitioners on financial instruments (chapter 4 of the 2007 SORP)
CIPFA Treasury management In local authorities – Icelandic banks collapse
Communities and Local Government Select Committee on local government investments, 11 June 2009
Audit Commission, risk and return, English local authorities and the Icelandic banks, March 2009; and
Fathom economic forecasts.
CIPFA Risk toolkit on Treasury management
Medium Term Financial Statement