

CYNGOR SIR POWYS COUNTY COUNCIL.

AUDIT COMMITTEE

7th February 2020

CABINET

11th February 2020

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Portfolio Holder for Finance**

REPORT TITLE: Treasury Management Quarter 3 Report

REPORT FOR: Information

1. Purpose

- 1.1 CIPFA's 2009 Treasury Management Bulletin suggested:
"In order to enshrine best practice it is suggested that authorities report formally on treasury management activities at least twice a year and preferably quarterly."

The CIPFA Code of Practice on Treasury Management emphasises a number of key areas including the following:-

- xi. Treasury management performance and policy setting should be subject to scrutiny prior to implementation.

- 1.2 In line with the above, this report is providing information on the activities for the quarter ending 31st December 2019.

2. Economic Background and Forecasts

- 2.1 The economic background is attached at Appendix B.
- 2.2 The most recent forecast of interest rates by the Authority's advisor is as follows:

	Mar 20	Jun 20	Sep 20	Dec 20	Mar 21	Jun 21	Sep 21
Bank rate	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%
5yr PWLB	2.40%	2.40%	2.50%	2.50%	2.60%	2.70%	2.80%
10yr PWLB	2.70%	2.70%	2.70%	2.80%	2.90%	3.00%	3.10%
25yr PWLB	3.30%	3.40%	3.40%	3.50%	3.60%	3.70%	3.70%
50yr PWLB	3.20%	3.30%	3.30%	3.40%	3.50%	3.60%	3.60%

3. Treasury Management Strategy

- 3.1 The Treasury Management Strategy approved by Full Council on 7th March 2019 is at Appendix A.
- 3.2 The Authority's investment priorities within the Strategy are: -
- (a) the security of capital and
 - (b) the liquidity of its investments.
- 3.3 The Authority aims to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite has been low in order to give priority to security of investments.

4. Current Investments

- 4.1 The current investment market is difficult in respect of earning the level of interest rates commonly seen in previous years as rates are very low and in line with the 0.75% Bank Rate.
- 4.2 The Authority had the following investments at 31st December 2019:-

Invested with:	Principal £000's	Interest Rate	Start Date	Maturity Date
HSBC	4,915	0.50%		
Thurrock BC	5,000	0.74%	30-Sep-19	06-Jan-20
Total	9,915			

- 4.3 Higher return rates have been difficult to achieve as the Authority is not in a position to invest its cash for more than a short period of time.
- 4.4 Investment returns in future years:
Our advisors' current suggested earning rates for investments for budgeting purposes were as follows:-

2019/20	0.75%
2020/21	0.75%
2021/22	1.00%

These are based on investments for up to three months duration.

5. Credit Rating Changes

- 5.1 There have been no credit rating changes relevant to this Authority's position during the last quarter.
- 5.2 The credit rating list for end of December is attached as a separate file to this report.

6. **Borrowing / Re-scheduling**

6.1 Effective management of the Authority's debt is essential to ensure that the impact of interest payable is minimised against our revenue accounts whilst maintaining prudent borrowing policies.

6.2 The Authority's Capital Position:

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the current year's unfinanced capital expenditure and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

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 the capital plans and cash flow requirements. This may be sourced through external borrowing or utilising temporary cash resources within the Council.

Net external borrowing (borrowings less investments) should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for the current year and next two financial years. This allows some flexibility for limited early borrowing for future years.

Original CFR Position (per original approved budget):

	As at 31.03.19 Actual	2019/20 Original Estimate	2020/21 Original Estimate	2021/22 Original Estimate
	£M	£M	£M	£M
Capital Financing Requirement	349,530	401,581	446,140	465,145

Updated CFR position as at 31.12.19:

	As at 31.03.19 Actual	2019/2020 Current Estimate	2020/21 Current Estimate	2021/22 Current Estimate
	£M	£M	£M	£M
Capital Financing Requirement	349,530	392,125	440,252	478,869

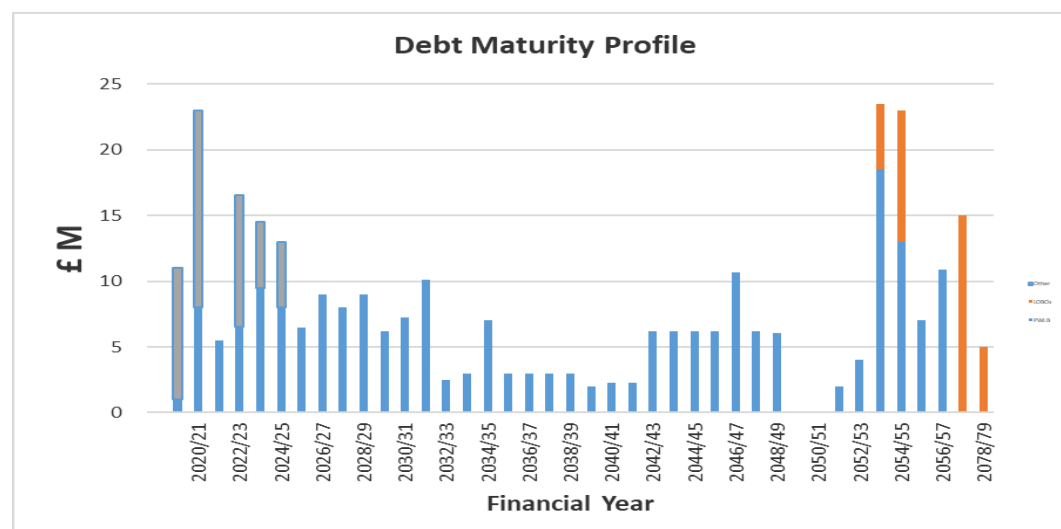
- 6.3 The Authority had outstanding long-term external debt of £299.2m at 31st March 2019. In relation to the CFR figure for 31st March 2019, this equated to the Authority being under borrowed by £50.3m. Using cash reserves as opposed to borrowing has been a prudent and cost effective approach over the last few years. However, members will be aware that internal borrowing is only a temporary situation and officers have advised that, based on capital estimates, it will be necessary for the Authority to borrow at stages over the next few years.
- 6.5 On 9th October 2019 HM Treasury increased the margin that applies to new PWLB loans by 100bps with no prior discussion. This led to increased borrowing rates for local authorities.
- 6.4 Capital Budget/Spend per efincials:

Capital:	Original Approved Budget £	Working Budget £	Actual Capital Spend (not including commitments) £	%age Actual Spend
	92,234,000			
Qtr 1 end of June		123,568,153	6,655,314	5.39%
Qtr 2 end of Sept		102,036,287	21,973,109	21.53%
Qtr 3 end of Dec		76,226,654	39,298,294	51.55%

The financing of the approved capital budget included £51m of Prudential Borrowing and Supported Borrowing of £13.72m.

It remains a significant challenge to manage the Authority's cashflow and its need to borrow when the Capital working budget increases/decreases significantly during the financial year and, despite this, actual spend continues to be significantly below the working budget.

6.5 Debt Maturity Profile as at 31.12.19:



6.6 PWLB Loans Rescheduling:

The Public Works Loans Board released a circular regarding rates on 20th October 2010. As a result of this, rates immediately increased by 0.87-0.88 basis points across the board. The overall impact of this circular was that it is far more difficult for authorities to reschedule debt. PWLB interest rates in the last quarter have not been conducive towards any rescheduling.

7. **Prudential Indicators**

- 7.1 All TM Prudential Indicators were complied with in the quarter ending 31st December 2019.

8. **VAT**

- 8.1 The Technical Section of Finance act as the authority's VAT section. VAT can pose a risk to the authority hence the Treasury Manager has been asked to include VAT information in these quarterly reports.
- 8.2 The monthly VAT returns were submitted within the required deadlines during the quarter ending 31st December 2019.
- 8.3 Key Performance Indicators:

The VAT KPI's for 2019/20 are attached at Appendix C. The KPI's for debtor invoices are showing an improvement compared to previous years due to the introduction of a workflow process for checking debtor invoices implemented as part of the new financial system in April. Further to this, this process is now ensuring correct vat treatment prior to invoices being raised as opposed to after.

Advice

N/A

Resource Implications

N/A

Legal implications

N/A

Comment from local member(s)

N/A

Integrated Impact Assessment

N/A

Recommendation

It is recommended that this report be accepted.

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Appendix A:

Approved Treasury Management Strategy 2019/20:

7.5 “High” credit quality:

- 7.5.1 It is proposed that the Authority continue with the following in respect of defining a “high” credit quality. If a rating is not available from any of the rating agencies then the available ratings will be used. Members will note that this proposal excludes investments with some banks off the advisors’ suggested list:-

Long Term Ratings (in respect of long-term investments):

Permitted Fitch Ratings	Permitted Moody's Ratings	Permitted S&P Ratings
AAA	Aaa	AAA
AA+	Aa1	AA+
AA	Aa2	AA
AA-	Aa3	AA-

Short Term Ratings (in respect of short-term investments):

Permitted Fitch Ratings	Permitted Moody's Ratings	Permitted S&P Ratings
F1+	N/A	A-1+
F1	P-1	A-1

7.6 Country limits:

- 7.6.1 It is proposed that the Authority will use approved counterparties from the UK and approved counterparties from other countries with the following sovereign credit ratings:-

Permitted Fitch Ratings	Permitted Moody's Ratings	Permitted S&P Ratings
AAA	Aaa	AAA

Country	Maximum Investment per Country	Credit Rating/Other Assessment of Risk
AAA countries	£20M (held in call accounts)	As per rating list
UK	No Maximum Investment	As per rating list

7.7 *Group/Institutions - Counterparty Criteria/Limits:*

Specified Investments:

Institution	Maximum Investment per Group/Institution £M	Maximum Length	Credit Rating/Other Assessment of Risk
UK Banks	30	Up to 364 days	As per Link's matrices and the Authority's definition of a high credit rating
Foreign Banks	5	Up to 364 days	As per Link's matrices and the Authority's definition of a high credit rating
Other Local Authorities	25	Up to 364 days	N/A

Non-Specified Investments:

Institution	Maximum Investment per Group/Institution £M	Maximum Length	Credit Rating/Other Assessment of Risk
UK Banks	10 (£5M limit with any one institution)	Up to 2 years	As per Link's matrices and the Authority's definition of a high credit rating
Foreign Banks	2	Up to 2 years	As per Link's matrices and the Authority's definition of a high credit rating
Money Market Funds (max. of 5)	10	N/A	All are AAA rated
Other Local Authorities	10	Up to 5 years	N/A
<i>Note: Limits for Specified and Non-Specified are combined limits. The maximum limit will also apply to a banking group as a whole.</i>			

Appendix B

Economic Background

UK

Economic growth in 2019 has been very volatile with quarter 1 unexpectedly strong at 0.5%, quarter 2 down at -0.2%, quarter 3 back up to +0.4% and quarter 4 expected to come in around zero. Political and Brexit uncertainty have dampened growth in 2019.

Despite political uncertainty ending with a decisive overall majority for the Conservative government in the December general election which clears the way for the UK to leave the EU on 31 January 2020, we still have much uncertainty as to whether there will be a reasonable trade deal achieved by the end of 2020.

After the Monetary Policy Committee raised Bank Rate from 0.5% to 0.75% in August 2018, it is little surprise that they have abstained from any further increases since then. We are unlikely to see any further action from the MPC until these remaining uncertainties over the likely type of Brexit become clear. If there was a no deal exit, it is likely that Bank Rate would be cut in order to support growth. However, if growth was to flag significantly in any event, the MPC could also cut Bank Rate in 2020. The Government has announced some major spending increases and is expected to make further commitments in the spring budget; these will provide some support to growth and will take some pressure off the MPC to act to stimulate growth by either cutting Bank Rate or implementing other monetary policy measures.

The MPC did have some concerns over the trend in wage inflation, which was on a rising trend, and peaked at a new post financial crisis high of 3.9% in June. Since then, however, it has been falling steadily back to 3.5% in October, (3 month average figure, excluding bonuses). Growth in employment picked up again to 24,000 in the three months to October, after a fall in the previous month's figures. However, this is still well below the 2018 average, although the unemployment rate remained at 3.8 percent, its lowest rate since 1975.

As for CPI inflation itself, this fell to 1.5% in October and November and is likely to remain between 1.5% and 2% over the next two years. If there was a no deal Brexit though, it could rise towards 4%, primarily as a result of imported inflation on the back of a weakening pound.

The strong wage inflation figure and the fall in CPI inflation is good news for consumers as their spending power is improving in this scenario as the difference between the two figures is now around 2.0%, i.e. a real term increase. Given the UK economy is very much services sector driven, an increase in household spending power is likely to feed through into providing some support to the overall rate of economic growth in the coming months.

Appendix C

VAT - Key Performance Indicators:

Creditor Invoices

VAT return for	No of high value Creditor invoices checked	No of Creditor invoices highlighted as requiring "proper" document for VAT recovery	%age of creditor invoices checked requiring "proper" document for VAT recovery
Apr-19	102	3	2.94%
May-19	184	1	0.54%
Jun-19	224	0	0.00%
Jul-19	235	1	0.43%
Aug-19	226	1	0.44%
Sep-19	177	1	0.56%
Oct-19	199	2	1.01%
Nov-19	214	2	0.93%
Dec-19			
Jan-20			
Feb-20			
Mar-20			

Income Management Entries

VAT return for	No of entries checked by formula per the ledger account code used	No of entries needing follow up check (but not necessarily incorrect)	%age of entries needing follow up check
Apr-19	645	17	2.64%
May-19	676	4	0.59%
Jun-19	947	3	0.32%
Jul-19	974	7	0.72%
Aug-19	590	12	2.035
Sep-19	877	13	1.48%
Oct-19	1,088	5	1.01%
Nov-19	893	13	1.46%
Dec-19			
Jan-20			
Feb-20			
Mar-20			

Debtor Invoices

VAT return for	No of Debtor invoices checked	No of checked debtor invoices with incorrect VAT code used	%age of debtor invoices with incorrect VAT code
Apr-19	50	0	0.00%
May-19	57	1	1.75%
Jun-19	72	6	8.33%
Jul-19	119	23	19.33%
Aug-19	74	3	4.05%
Sep-19	89	11	12.36%
Oct-19	59	5	8.47%
Nov-19	81	8	9.88%
Dec-19			
Jan-20			
Feb-20			
Mar-20			

Purchase Cards

VAT return for	No of transactions for previous month for which paperwork requested for checking	No of Amazon invoices included in check	Resolvable errors discovered	No of transactions for which no response received within timescale	Value of VAT potentially claimable but recharged to budget due to non-response	No of transactions where VAT claimed incorrectly	%age of transactions available to be checked where VAT was claimed incorrectly	Value of VAT incorrectly claimed hence recharged to budget
Apr-19	243	26	15	12	£1,161.13	11	4.76%	£1,162.23
May-19	302	25	21	20	£1,849.63	22	7.80%	£1,035.51
Jun-19	348	23	31	16	£1,677.68	12	3.61%	£730.63
Jul-19	279	0	19	11	£1,331.95	9	3.365	£1,856.52
Aug-19	132	0	9	4	£726.08	6	4.69%	-£35.05
Sep-19	256	0	15	11	£1,503.81	9	3.67%	£4,703.92
Oct-19	274	0	8	6	£1,170.47	10	3.73%	£1,799.96
Nov-19	266	0	9	N/A	N/A	N/A	2.63%	-£124.05
Dec-19								
Jan-20								
Feb-20								
Mar-20								

Chargebacks to service areas

The upload of appropriate documents to the Barclaycard purchase card system to enable vat recovery was made mandatory in September 2017 as a result of the lack of response from service areas/establishments to provide documents when requested. Where no document has been uploaded, any VAT amount input against the transaction is charged to the service area as there is no evidence to support the vat recovery.

Any other VAT errors that come to light as a result of the various checks are also charged to the relevant service areas.

Budget holders are able to see this clearly as chargebacks are coded to account code EX400600 and the activity code used alongside this gives the reason why this chargeback has occurred.

The total amount charged back to service areas in 2019/20 to end of December is £4,279.11. The breakdown of this is as follows:-

Reason	£
Not a tax invoice	3,018.05
Not a tax invoice – no response from service area	114.83
PCC not the named customer	4,328.81
No VAT registration number on invoice	142.00
No invoice uploaded to Barclaycard system	14,987.97
Invoices uploaded do not match the payment	512.31
No evidence supplied to enable vat recovery	634.20
Foreign VAT (not recoverable)	68.05
No VAT amount on invoice in first place	3,150.41
Supplier not vat registered	155.40
Supply not to PCC	12,012.83
Overaccounting for VAT	4,844.38
PCC Internal payment	0
Document spoilt	0
Pool car adjustment	776.58
Total	44,745.82

Of the above the £23,738.17 was potentially recoverable.