BRIDGEND COUNTY BOROUGH COUNCIL

REPORT TO CABINET

18 SEPTEMBER 2018

REPORT OF THE INTERIM HEAD OF FINANCE & SECTION 151 OFFICER

ANNUAL TREASURY MANAGEMENT OUTTURN REPORT 2017-18

1. Purpose of the Report

1.1 The purpose of the report is to:-

- Comply with the requirement of the Chartered Institute of Public Finance and Accountancy 'Treasury Management in the Public Services: Code of Practice' (the Code) to report an overview of treasury activities for the preceding financial year;

- Report on the actual Treasury Management and Prudential indicators for 2017-18.

2. Connection to Corporate Improvement Objectives/Other Corporate Priorities

2.1 This report assists in the achievement of the following corporate priority:

- *Smarter use of resources* – ensuring that all its resources (financial, physical, human and technological) are used as effectively and efficiently as possible and support the development of resources throughout the community that can help deliver the Council's priorities.

2.2 The Annual Treasury Management Outturn Report is integral to the delivery of the Corporate Improvement Objectives as the allocation of resources determines the extent to which the Corporate Objectives can be delivered.

3. Background

3.1 The Council's Treasury Management activities are regulated by the Local Government Act 2003 which provides the powers to borrow and invest as well as providing controls and limits on this activity. The Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 as amended, develops the controls and powers within the Act. This requires the Council to undertake any borrowing activity with regard to the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code for Capital Finance in Local Authorities and to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services. In March 2018 the

Welsh Government published an amendment to the Local Authorities (Capital Finance and Accounting) (Wales) Regulations which enables the Council to invest in certain instruments from 2017-18, which were previously treated as capital expenditure, without the potential revenue cost of Minimum Revenue Provision (MRP) and without the proceeds from sale being considered a capital receipt.

3.2 The Council is required to operate the overall treasury function with regard to the Code and this was formally adopted by the Council in February 2012. This includes a requirement for the Council to approve a Treasury Management Strategy (TMS) before the start of each financial year which sets out the Council's and Chief Financial Officer's responsibilities, delegation and reporting arrangements. Council approved the TMS 2017-18 on 1 March 2017. CIPFA published new editions of Treasury Management in the Public Services: Code of Practice and the Prudential Code for Capital Finance in Local Authorities in late December 2017 however the TMS 2017-18 and this report has been produced using the 2011 Codes. The Code also requires that Council receives an Annual Report after the close of the financial year.

3.3 The Welsh Government (WG) issued revised Guidance on Local Authority Investments in April 2010, which requires the Council to approve an Investment Strategy prior to the start of each financial year and this is included in the TMS.

3.4 This Annual Report covers the following areas for 2017-18:

- The Council's external debt and investment position
- Treasury Risk Management
- External Context
- Borrowing Strategy & Outturn
- Investment Strategy & Outturn
- Performance Measurement
- Review of the Treasury Management Strategy
- Reporting Arrangements
- Treasury Management and Prudential Indicators

4. Current Situation / Proposal

4.1 External Debt and Investment Position 2017-18

4.1.1 The Council's external debt and investment position for 1 April 2017 to 31 March 2018 is shown below in table 1; more detail is provided in section 4.4 the Borrowing Strategy and Outturn and section 4.5 the Investment Strategy and Outturn.

Table 1: Council's external debt and investment position 1 April to 31 March 2018

	Principal as at 01-04-17 £m	Average Rate 01-04-17 %	Principal as at 31-03-18 £m	Average Rate 31-03-18 %
External long term borrowing:				
Public Works Loan Board (PWLB)	77.62	4.70	77.62	4.70
Lender's Option Borrower's Option (LOBO)	19.25	4.65	19.25	4.65
Total external borrowing	**96.87**	**4.69**	**96.87**	**4.69**
Other long term liabilities (LTL)				
Private Finance Initiative (PFI)*	18.24		17.64	
Llynfi Loan**	2.40		2.40	
Other LTL	1.13		0.98	
Total other long term liabilities	**21.77**		**21.02**	
Total gross external debt	**118.64**		**117.89**	
Treasury investments:				
Banks	8.25	0.55	7.40	0.58
Building Societies	6.00	0.38	2.00	0.54
Government (including Local Authorities)	19.50	0.60	21.00	0.64
Total treasury investments	**33.75**	**0.55**	**30.40**	**0.62**
Net Debt	**84.89**		**87.49**	

***** (PFI) arrangement for the provision of a Secondary School in Maesteg 16 years remaining term
** loan from the WG Central Capital Retained Fund for regeneration works within the Llynfi Valley which has not yet commenced

4.1.2 It should be noted that the accounting practice to be followed by the Council requires financial instruments in the accounts (debt and investments) to be measured in a method compliant with International Financial Reporting Standards (IFRS). The figures shown in the table above and throughout the report are based on the actual amounts borrowed and invested and so may differ from those in the Statement of Accounts which include accrued interest or are stated at fair value in different instances.

4.1.3 The £19.25 million in the above table relates to Lender's Option Borrower's Option (LOBO) loans due to mature in 2054, which may be re-scheduled in advance of this maturity date. The LOBO rate and term may vary in the future depending upon the prevailing market rates, the lender exercising their option to increase rates at one of the bi-annual trigger points (the trigger dates being July and January) and therefore, the Council being given the option to accept the increase or to repay the loan without incurring a penalty. Following advice from Arlingclose, the Council approached the LOBO's lender for potential repayment options in 2017-18, however the premium was deemed too excessive to action. The first trigger point in 2018-19 was July 2018 and the lender did not exercise this option in the current low interest rate environment, however an element of refinancing risk remains and the Council would take the option to repay these loans at no cost if it has the opportunity to do so in the future. The current average interest rate for these LOBO's is 4.65% compared to the PWLB Loans average interest rate of 4.70%.

4.1.4 The long term liabilities figure of £21.02 million at 31 March 2018 includes £17.64 million for the Council's Private Finance Initiative (PFI) arrangement (for the provision of a Secondary School in Maesteg - sixteen years remaining term) which includes the short term PFI liability of £0.64 million which is included as current liabilities in the Council's balance sheet in the Statement of Accounts. Also included is £2.40 million relating to a loan from the WG Central Capital Retained Fund for regeneration works within the Llynfi Valley which has not yet commenced.

4.1.5 Favourable cash flows have provided surplus funds for investment and the balance on investments at 31 March 2018 was £30.40 million (average interest rate 0.62%). This was a decrease from the start of the financial year where investments were £33.75 million (average interest rate 0.55%). Table 2 in section 4.5 details the movement of the investments during 2017-18 by counterparty types and shows the average balances, interest received, duration and rates for the year.

4.1.6 The treasury management function has been reviewed by the Council's External Auditors, the Wales Audit Office during the 2017-18 annual audit and there were no adjustments relating to treasury management. In addition to the External Audit work, Internal Audit undertook an audit of the treasury management function during 2017-18 and the audit identified that "based on an assessment of the strengths and weakness of the areas examined, and through testing it has been concluded that the effectiveness of the internal control environment is considered to be sound and therefore substantial assurance can be placed upon the management of risks".

4.1.7 The Council's treasury management advisors are Arlingclose. Their contract runs from 1 September 2016 for four years following a tender process and the contract will be reviewed annually and either party may at any time terminate this agreement on 3 months prior written notice. The current services provided to the Council include:-

- advice and guidance on relevant policies, strategies and reports
- advice on investment decisions
- notification of credit ratings and changes
- other information on credit quality
- advice on debt management decisions

- accounting advice
- reports on treasury performance
- forecasts of interest rates
- training courses.

4.2 Treasury Risk Management 2017-18

4.2.1 The TMS sets out the parameters for the management of risks associated with Financial Instruments. The Council also produces Treasury Management Practices specifying the practical arrangements to be followed to manage these risks. The Council's overall treasury risk management procedures focus on the unpredictability of financial markets and implementing restrictions to minimise these risks.

4.2.2 The Council's activities expose it to a variety of financial risks, the key risks are:-

- Credit risk (i.e. security) – the possibility that other parties might fail to pay amounts due to the Council;
- Liquidity risk – the possibility that the Council might not have funds available to meet its commitments to make payments;
- Market risk - the possibility that financial loss might arise for the Council as a result of changes in such measures as interest rates movements.

4.2.3 The Council's primary objective for the management of its investments is to give priority to the security and liquidity of its funds before seeking the best rate of return so not all the options available to the Council were utilised during 2017-18. The majority of the Council's surplus funds during 2017-18 were therefore kept in the form of short-term investments and were all placed with counterparties satisfying the appropriate credit criteria and spread over a number of counterparties. This was deemed a much safer option even though it may be at the expense of extra basis points in interest and more detail is provided below in section 4.5.

4.2.4 The counterparty limits were constantly reviewed and where market conditions dictated, the limit was dropped below the limits detailed in the Investment Strategy. No breaches of the Council's counterparty criteria occurred during 2017-18 and the Council does not expect any losses from non-performance by any of its counterparties in relation to deposits**.** A risk of irrecoverability applies to all of the Council's deposits, but there was no evidence at the 31 March 2018 that this was likely to crystallise. Table 3 below in section 4.5 summarises the credit risk exposures of the Council's investment portfolio by credit rating, based on the lowest long term rating.

4.3 External Context 2017-18

4.3.1 The interest rate views, incorporated in the Council's TMS 2017-18, were based upon officers' views supported by a selection of City forecasts provided by Arlingclose. When the TMS 2017-18 was prepared in January 2017 it was forecast that the Bank Rate would remain at 0.25% during 2017-18 with a low possibility of a drop close to zero and with a very small chance of a reduction below zero.

4.3.2 The Bank Rate started the financial year at 0.25% and the Bank of England's Monetary Policy Committee (MPC) increased this by 0.25% to 0.50% in November 2017. It was significant in that it was the first rate hike in ten years, although in essence the MPC reversed its August 2016 cut following the EU referendum result. The Bank Rate remained at 0.50% for the remainder of 2017-18.

4.4 Borrowing Strategy and Outturn 2017-18

4.4.1 Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. The uncertainty over future interest rates increases the risks associated with treasury activity. As a result the Council took a cautious approach to its treasury strategy. With short-term interest rates currently lower than long term rates, it is likely to be more cost effective in the short term to either borrow short term or use internal resources. Short term and variable rate loans expose the Council to the risk of short term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates as shown in the treasury management indicators in section 4.9 and **Appendix A**. However, with long term rates forecast to rise in the coming years, any such short term savings will need to be balanced against the potential longer-term costs. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis.

4.4.2 The Council's primary objective for the management of its debt is to ensure its long term affordability. The majority of its loans have therefore been borrowed from the Public Works Loan Board (PWLB) at long term fixed rates of interest and the last time the Council took long term borrowing was £5 million from the PWLB in March 2012. The premium charge for early repayment of PWLB debt remained relatively expensive for the loans in the Council's portfolio and therefore unattractive for debt rescheduling activity so no rescheduling activity was undertaken in 2017-18 as a consequence, however, in conjunction with Arlingclose, the loan portfolio will continue to be reviewed for any potential savings as a result of any loan rescheduling. For cash-flow purposes on two occasions short term borrowing was taken in 2017-18 totalling £4 million and repaid within a month and there was none outstanding at 31 March 2018.

4.4.3 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This is known as Internal Borrowing. This strategy is prudent as investment returns are low and counterparty risk is relatively high.

4.5 Investment Strategy and Outturn 2017-18

4.5.1 Both the CIPFA Code and the WG Guidance require the Council 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 Council's objective when investing money is to strike an appropriate balance between risk and return, balancing the risk of incurring losses from defaults against receiving unsuitably low investment income. The Annual Investment Strategy incorporated in the Council's TMS 2017-18 includes the credit ratings defined for each category of investments, the prudential use of non-specified investments and the liquidity of investments.

4.5.2 Investment decisions are made by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's to ensure that this lies within the Council's agreed minimum credit rating. **Appendix B** shows the equivalence table for these published credit ratings and explains the different investment grades. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. In the current climate, relying mainly on credit ratings is considered to be inappropriate and the Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

4.5.3 The Council's investments have historically been placed in bank and building society unsecured deposits and local and central government, however, investments may be made with any public or private sector organisations that meet the minimum credit criteria specified in the Investment Strategy. The Council is diversifying into more secure and/or higher yielding asset classes and any new instruments used will be in full consultation with Arlingclose. In order to be able to use the majority of these different types of instruments, the Council is required to use a nominee account(s) with a third party for safe custody of such investments (a custody account) as they cannot be dealt direct. On 5 September 2017, Cabinet approved the opening of a King & Shaxson custody account. It also delegated authority to the Section 151 Officer, in consultation with the Monitoring Officer, to open additional custody accounts to support delivery of treasury management responsibilities if required. The custody account was used in October 2017 to invest in a £1 million HM Treasury bill which matured in January 2018.

4.5.4 The Council opened a Money Market Fund in August 2017 with the Churches, Charities and Local Authorities (CCLA) Public Sector Deposit Fund which is a pooling of public sector deposits wholly aligned with the principles and values of the public sector. It is UK domiciled, regulated by the Financial Services Authority with an advisory board representing the public sector depositors which ensures strong governance arrangements of the Fund. This is an approved financial instrument in the TMS 2017-18 and provides instant access to the funds. There was no balance outstanding at 31 March 2018.

4.5.5 On a day to day basis the Council potentially has positive cash balances arising from the cash flow e.g. timing differences between grants being received and making various payments. These are invested on the market via brokers, direct with the institution or held in deposit accounts. The Council usually invests for a range of periods dependent on cash flow requirements and the interest rates on offer having regard to the Investment Strategy. There were two new long term investments (original duration of 12 months or more) made with local authorities in 2017-18 both for two years totalling £5 million but all other investments in 2017-18 were short term. The table below details the investments in 2017-18 by counterparty type:-

Table 2: Investments Profile 2017-18

Investment Counterparty Category	Balance 01 April 2017 (A) £m	Investments Raised (B) £m	Investments Repaid (C) £m	Balance 31 March 2018 (A+B-C) £m	Interest Received 2017-18 £'000	Average Original Duration of the Investment Days	Weighted Average Investment Balance 2017-18 £m	Weighted Average Interest Rate 2017-18 %
Government - DMO	-	134.40	134.40	-	3.76	6	2.04	0.18
Government Treasury Bill	-	1.00	1.00	-	0.67	91	0.25	0.27
Local Authorities	19.50	143.60	142.10	**21.00**	155.53	130	30.52	0.51
Building Societies	6.00	10.00	14.00	**2.00**	19.12	128	3.87	0.39
Banks (Fixed Maturity)	3.00	11.00	9.00	**5.00**	25.45	213	6.49	0.62
Banks Instant Access/Notice Period Accounts*	5.25	97.16	100.01	**2.40**	21.85	n/a	5.44	0.40
Money Market Fund (Instant Access)*	-	11.30	11.30	-	2.65	n/a	1.02	0.29
Total/Average	**33.75**	**408.46**	**411.81**	**30.40**	**229.03**	**113**	**49.63**	**0.49**

* An average duration is not shown as there is no original duration as instant access or notice period and money is added and withdrawn to/from these accounts as required by cash-flow

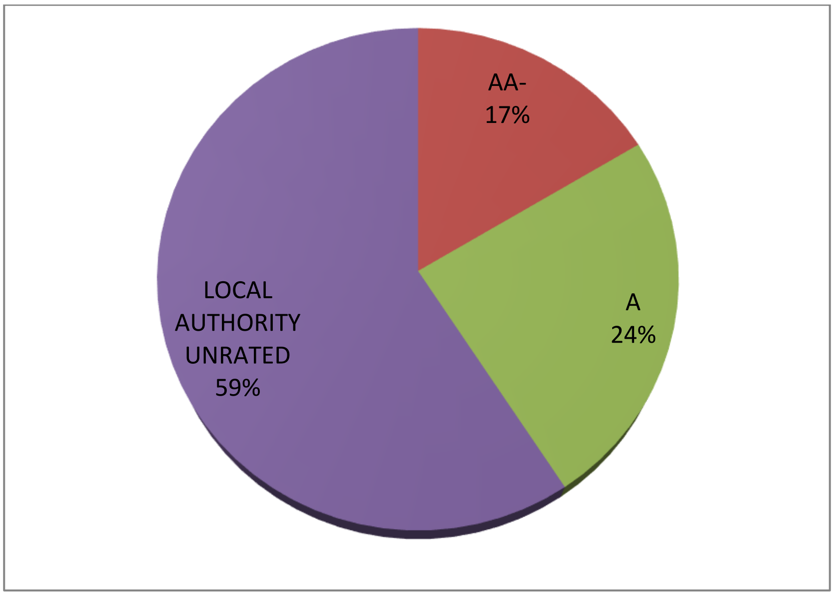
4.5.6 Occasionally, investments are placed with the UK Debt Management Office (DMO - Executive Agency of UK Government) but only for very short term deposits (as shown in table 2 above) and only as a last resort as the interest rates offered by this facility are lower than some other counterparties but this is commensurate with the high level of security and reduced risk offered. It provides another option when examining potential investments and ensures compliance with the Council's investment objective that security takes priority over yield. There were no deposits outstanding with the DMO at 31 March 2018.

4.5.7 Favourable cash flows have provided positive cash balances for investment and as shown above the balance on investments at 31 March 2018 was £30.40 million made up of £9 million long term investments, £20 million short term investments and £1.40 million Cash and Cash Equivalents. Table 3 below summarises the credit risk exposure of the Council's £30.40 million investments at 31 March 2018 by credit rating, (based on the lowest long term rating) maturity profile (remaining duration from 31 March 2018) and counterparty type:-

Table 3: Investments Outstanding Maturity Profile 31 March 2018

Counterparty Category	Credit Rating	Instant Access Deposit Account £m	Notice Period Deposit Account £m	Deposits Maturing within 1 Month £m	Deposits Maturing Within 2 to 6 Months £m	Deposits Maturing Within 7 Months up to 1 Yr. £m	Deposits Maturing Within 1 to 3 Yrs. £m	Total 31-3-18 £m
Bank	AA-				2.00			**2.00**
Bank	A	1.40	1.00	2.00	1.00			**5.40**
Building Societies	A				2.00			**2.00**
Local Authorities	AA-						3.00	**3.00**
Local Authorities unrated				2.00	9.00	1.00	6.00	**18.00**
Total		**1.40**	**1.00**	**4.00**	**14.00**	**1.00**	**9.00**	**30.40**

4.5.8 The Council defines high credit quality as organisations and securities having a credit rating of A- or higher. The pie chart below summarises the above table by credit ratings and shows the £30.40 million investments at 31 March 2018 by percentage outstanding. Most Local Authorities do not have credit ratings and the remainder of the Council's investments all had a credit rating of A or above.



4.6 Performance Measurement 2017-18

4.6.1 The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury function over the year and the ones set in the TMS 2017-18 are shown below. These are distinct historic indicators as opposed to the Treasury Management and Prudential Indicators (shown below in section 4.9 and Appendix A) which are predominantly forward looking. One debt performance indicator is where the average portfolio rate of interest is compared to an appropriate average available such as the average PWLB Debt for Welsh and UK Local Authorities.

4.6.2 The average long term borrowing rate for 2017-18 and at 31 March 2018 was 4.69% (the same rate as at 31 March 2017) and 80% of this was made up of Public Works Loan Board (PWLB) loans with an average rate of 4.70% (the same rate as at 31 March 2017). Comparable performance indicators are shown below:-

Bridgend CBC Average Rate of PWLB Debt 31-03-18 %	**All Welsh Local Authorities* Average Rate for outstanding PWLB Debt 31-03-18 %**	**All UK Local Authorities* Average Rate for outstanding PWLB Debt 31-03-18 %**
4.70	4.75	4.07
	-0.05	**+0.63**

*excluding Parish, Town and Community Councils

4.6.3 The average rate on investments for 2017-18 was 0.49% and at 31 March 2018 was 0.62% (compared to 0.49% for 2016-17 and 0.55% at 31 March 2017). Comparable performance indicators for benchmarking purposes set in the TMS 2017-18 were the average 1 month London Inter Bank Bid (LIBID) rate and the average Bank Rate. The tables below show the investments average interest rate for 2017-18 and the actual rate as at 31 March 2018 compared favourably against these two benchmarking rates:

Bridgend CBC Average Rate of Return on Investments 2017-18 %	**Average 1 month LIBID (London Inter-Bank Bid rate) 2017-18 %**	**Average Bank Rate 2017-18** %
0.49	0.23	0.35%
	+0.26	**+0.14**
Bridgend CBC Average Rate of Return on Investments 31-03-18 %	**1 month LIBID (London Inter-Bank Bid rate) 31-03-18 %**	**Bank Rate 31-03-18 %**
0.62	0.39	0.50
	+0.23	**+0.12**

4.6.4 The Council participates in a benchmarking exercise with Arlingclose. As shown below, the Council's average rate of return on investments at the end of each quarter in 2017-18 was more favourable compared to the average of Arlingclose Welsh Local Authorities Unitary clients:

2017-18	Principal £m	Bridgend CBC Average Rate of Return on Investments %	Principal £m	Arlingclose Clients Welsh Unitaries Average Rate of Return on Investments %
30-06-17	47.10	**0.45**	31.60	0.40
30-09-17	44.00	**0.48**	25.90	0.29
31-12-17	43.30	**0.58**	30.00	0.44
31-03-18	30.40	**0.62**	31.00	0.47

4.7 Review of the Treasury Management Strategy 2017-18

4.7.1 CIPFA's Code of Practice for Treasury Management requires all local authorities to conduct a mid-year review of its treasury management policies, practices and activities. As a result of this review it was not deemed necessary to make any major changes to the TMS 2017-18.

4.8 Reporting Arrangements 2017-18

4.8.1 CIPFA's Code of Practice for Treasury Management requires that the Council reports on its treasury management as an annual strategy and plan in advance of the year, a mid-year review and an annual outturn report after its close to Council. The Council also produces quarterly monitoring reports that go to Cabinet as Information Reports. The Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Cabinet, and for the execution and administration of treasury management decisions to the Section 151 Officer, who will act in accordance with the Council's TMS and CIPFA's Standard of Professional Practice on Treasury Management.

4.8.2 The Council has complied with its legislative and regulatory requirements during 2017-18. The TMS 2017-18 and the Half Yearly Outturn were reported to Council on 1 March 2017 and 1 November 2017 respectively and this Annual Treasury Management Outturn Report is being reported to Cabinet and Council in September 2018. In addition, quarterly monitoring reports were presented to Cabinet during 2017-18.

4.8.3 To ensure effective scrutiny of treasury management in accordance with the TMS, Audit Committee has been nominated to be responsible for ensuring effective scrutiny of the TMS and policies. Audit Committee received training in June 2017 to assist them in their function of scrutinising treasury management, with particular emphasis on investment options available to the Council and Elected Members were also invited to attend.

4.8.4 During the 2017-18 financial year, in addition to the regular treasury management reports to Cabinet and Council, Audit Committee received the Annual Treasury Management Report 2016-17 in June 2017, the Half Year Treasury Management Report 2017-18 in November 2017, the TMS 2018-19 in January 2018 and an Annual Outturn Report 2017-18 in June 2018.

4.9 Treasury Management & Prudential Indicators 2017-18

4.9.1 The Treasury Management Code and Prudential Code require the Council to set and report on a number of Treasury Management and Prudential Indicators. Details are shown in **Appendix A** of the estimated indicators for 2017-18 as detailed in the TMS 2017-18 approved by Council 1 March 2017, the revised projection (where applicable) as set out in the TMS 2018-19 approved by Council 28 February 2018, and the actual indicators for 2017-18.

4.9.2 In 2017-18, the Council operated within the limits and indicators as set out in the agreed TMS 2017-18 and complied with its treasury management practices.

5. Effect upon Policy Framework & Procedure Rules

5.1 As required by Financial Procedure Rule 20.3 within the Council's Constitution, all investments and borrowing transactions have been undertaken in accordance with the TMS 2017-18 as approved by Council with due regard to the requirements of the CIPFA's Code of Practice on Treasury Management in the Public Services.

6. Equality Impact Assessment

6.1 There are no equality implications.

7. Well-being of Future Generations (Wales) Act 2015 Implications

7.1 The well-being goals identified in the Act were considered in the preparation of this report. As the report is for information only it is considered that there will be no significant or unacceptable impacts upon the achievement of well-being goals/objectives as a result of this report.

8. Financial Implications

8.1 The financial implications are reflected within the report.

9. Recommendation

9.1 It is recommended that Cabinet:

- Note the treasury management activities for 2017-18;
- Note the actual Treasury Management and Prudential Indicators for 2017-18.

Gill Lewis
Interim Head of Finance & Section 151 Officer
9 August 2018

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Background documents:

Treasury Management Strategy 2017-18
Treasury Management Strategy 2018-19

APPENDIX A

1 Treasury Management Indicators 2017-18

1.1 The following indicators (which are forward looking parameters) form part of the CIPFA Code of Practice on Treasury Management. They enable the Council to measure and manage its exposure to Treasury Management risks.

The Council needs to set the upper limits to its **Interest Rate Exposure** for the effects of changes in interest rates. There are two treasury management indicators relating to both fixed interest rates and variable interest rates. These limits have been calculated with reference to the net outstanding principal sums and are set to control the Council's exposure to interest rate risk and are shown in the table below. Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or transaction date if later and all other instruments are classed as variable. The majority of the Council's investments are less than 12 months and even though interest rates may be fixed for the investment duration these would be classed as variable. LOBO loans are variable interest rate loans, therefore, as the investments were in excess of total variable rate loans, the variable interest rate exposure (net principal) is shown as negative in the table below.

The Section 151 Officer managed interest rate exposure between these limits during the year and as shown below the net borrowing position for fixed and variable rates was within the limits set.

No.	Interest Rate Exposure	TMS 2017-18 £m	Revised Projection 2017-18 TMS 2018-19 £m	Actual Outstanding 31-03-18 £m
	Total Projected Principal Outstanding on Borrowing 31 March 2018	96.87	96.87	**96.87**
	Total Projected Principal Outstanding on Investments 31 March 2018	24.00	30.00	**30.40**
	Net Principal Outstanding	**72.87**	**66.87**	**66.47**
1.	**Upper Limit on fixed interest rates (net principal) exposure**	130.00	**n/a**	**n/a**
2.	**Upper Limit on variable interest rates Exposure (net principal) exposure**	50.00	**n/a**	**n/a**
	Fixed interest rate exposure (net principal) 31 March 2018		**68.62**	**68.62**
	Variable interest rate exposure (net principal) 31 March 2018		**1.25**	**-2.15**

1.2 A further indicator for Treasury Management measures the **Maturity Structure of Borrowing** and is the amount of projected borrowing that is fixed rate, maturing in each period as a percentage of total projected fixed rate borrowing. This indicator is set to control the Council's exposure to refinancing risk and has been set to allow for the possible restructuring of long term debt where this is expected to lead to an overall saving or reduction in risk.

No	Maturity structure of fixed rate borrowing during 2017-18	Upper limit %	Lower limit %	Actual 31-03-18 %
3.	Under 12 months	50	0	**19.87**
	12 months and within 24 months	25	0	**-**
	24 months and within 5 years	25	0	**-**
	5 years and within 10 years	50	0	**13.91**
	10 years and within 20 years	60	0	**23.49**
	20 years and above	100	40	**42.73**

The 19.87% in the table above relates to £19.25 million Lender's Option Borrower's Option (LOBO) loans which may be re-scheduled in advance of their maturity date of 2054, as detailed in section 1 above. The Code requires the maturity of LOBO loans to be shown (even though the rate is variable) as the earliest date on which the lender can require payment, i.e. the next call date after 31 March 2018 which is July 2018, however, the lender did not exercise this option due to current low interest rates and the Council is not anticipating that this will occur during 2018-19 so the maturity date is actually uncertain but is shown in the "Under 12 months" category as per the Code.

1.3 The **Upper Limit for Total Principal Sums invested over 364 days** indicator controls the amount of longer term investments which mature beyond the period end. This is set to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments.

No.		TMS 2017-18 £m	Actual Principal Outstanding Over 364 days 31-03-18 £m
4.	**Upper Limit for Total Principal Sums Invested for more than 364 days**	15	**9**

The actual for all three treasury management indicators above are within the accepted range.

2. Prudential Indicators 2017-18

The Prudential Indicators are required to be set and approved by Council in accordance with CIPFA's Prudential Code for Capital Finance in Local Authorities.

Council is required to formally adopt CIPFA's Treasury Management Code and the revised edition of the 2011 code was adopted by Council on 22 February 2012.

2.1 Prudential Indicators for Prudence

2.1.1 The following Prudential Indicators are based on the Council's capital programme which is subject to change. The Council's capital expenditure plans are summarised below and this forms the first prudential indicator for Prudence. The total capital expenditure was funded from capital grants and contributions, capital receipts and revenue with the remainder being the **Net Financing Need for the Financial Year** to be met from borrowing.

No.	Prudential indicators For Prudence 2017-18	Estimate TMS 2017-18 £m	Revised Projection 2017-18 TMS 2018-19 £m	Actual 2017-18 £m
1.	**Estimates of Capital Expenditure** (Non-HRA)	63.85	45.41	**36.58**
	Total Capital Expenditure	**63.85**	**45.41**	**36.58**
	Financed by :-			
	Capital Grants and Contributions	24.37	15.14	**16.63**
	Capital Receipts	20.04	10.90	**0.18**
	Revenue contribution to Capital	9.92	9.61	**9.92**
	Net Financing Need for Year	**9.52**	**9.76**	**9.85**

The capital expenditure figures have changed from the TMS 2017-18 as the capital programme approved by Council on 1 March 2017 has been amended to include new approved schemes and to incorporate slippage of schemes identified as part of the capital monitoring which has resulted in a very small increase in the Net Financing Need for 2017-18.

The process for charging the financing of capital expenditure to revenue is a statutory requirement and is called the Minimum Revenue Provision (MRP). The actual MRP charge needs to be prudent and the methodology is detailed in the Council's MRP policy in the TMS 2017-18. Directorates who receive Council approval for capital schemes via Unsupported Borrowing make annual contributions to the capital costs of their schemes known as Voluntary Revenue Provisions (VRP) or additional MRP. This type of borrowing is only approved when Directorates have the necessary revenue resources to make VRP to fund the capital costs though this will be deferred in some cases until the asset becomes operational in accordance with the Council's MRP Policy.

2.1.2 The second Prudential Indicator is the Capital Financing Requirement (CFR) for the Council and is shown in the table below. This shows the total outstanding capital expenditure that has not been funded from either revenue or other capital resources. It is derived from the actual Balance Sheet of the Council. It is essentially a measure of the underlying need to finance capital expenditure and forms the basis of the charge to the General Fund in line with the Prudential Code.

The MRP requirement for the Maesteg School PFI Scheme and the Innovation Centre will be equivalent to the write down of the liability for the year and is met from existing budgets.

No.	Prudential indicators For Prudence	Estimate TMS 2017-18 £m	Revised Projection 2017-18 TMS 2018-19 £m	Actual 2017-18 £m
2.	**Capital Financing Requirement (CFR)**			
	Opening CFR (1 April 2017) adjusted excluding PFI & other liabilities	150.65	149.20	149.20
	Opening PFI CFR	18.24	18.24	18.24
	Opening Innovation Centre	0.66	0.66	0.66
	Opening Coychurch Crematorium	0.08	0.08	0.08
	Total Opening CFR	**169.63**	**168.18**	**168.18**
	Movement in CFR excluding PFI & other liabilities	2.90	**3.36**	3.44
	Movement in PFI CFR	(0.60)	(0.60)	(0.60)
	Movement in Innovation Centre CFR	(0.06)	(0.06)	(0.06)
	Movement in CREM CFR	(0.08)	(0.08)	(0.08)
	Total Movement in CFR	**2.16**	**2.62**	**2.70**
	Closing CFR (31 March 2018)	**171.79**	**170.80**	**170.88**
	Movement in CFR represented by :-			
	Net Financing Need for Year (above)	9.52	9.76	9.85
	Minimum and Voluntary Revenue Provisions*	(7.36)	(7.14)	(7.15)
	Total Movement	**2.16**	**2.62**	**2.70**

*Minimum Revenue Provision (MRP) and Voluntary Revenue Provision (VRP) represent the revenue charge for the repayment of debt and include MRP for the Public Finance Initiative (PFI) and the Innovation Centre

2.2 Limits to Borrowing Activity

2.2.1 The Council's long term borrowing at the 31 March 2018 was £96.87 million as detailed in section 1 of the main report. External Borrowing can arise as a result of both capital and revenue expenditure and timing of cash flows. As the Council has an integrated TMS there is no association between individual loans and particular types of expenditure. Therefore, the Capital Financing Requirement and actual external borrowing can be very different especially when a Council is using Internal Borrowing as highlighted in paragraph 4.4.3 in the main report

The **Gross Debt** position (Borrowing and Long Term Liabilities) is shown below.

No.	Prudential indicators For Prudence Gross Debt 2017-18	Estimate TMS 2017-18 £m	Revised Projection 2017-18 TMS 2018-19 £m	Actual Outstanding 31-03-18 £m
3.	External Borrowing	96.87	96.87	**96.87**
	Long Term Liabilities (including PFI)	21.07	20.99	**21.02**
	Total Gross Debt	**117.94**	**117.86**	**117.89**

2.2.2 Within the Prudential Indicators, there are a number of key indicators to ensure the Council operates its activities within well-defined limits. One key control is to ensure that over the medium term, debt will only be for a capital purpose. The Council needs to ensure that the external debt does not, except in the short term, exceed the Capital Financing Requirement for 2017-18. The table below shows that the Council has complied with this requirement.

No.	Prudential indicators For Prudence 2017-18	Estimate TMS 2017-18 £m	Revised Projection 2017-18 TMS 2018-19 £m	Actual Outstanding 31-03-18 £m
4.	**Gross Debt & the CFR**			
	Total Gross Debt	117.94	117.86	**117.89**
	Closing CFR (31 March)	**171.79**	**170.80**	**170.88**

2.2.3 A further two Prudential Indicators detailed below control the Council's overall level of debt to support Capital Expenditure and were well within the limit set:

The Authorised Limit for External Debt – this represents the limit beyond which borrowing is prohibited. It reflects a level of borrowing that could not be sustained even though it would be affordable in the short term. It needs to be set and approved by Members.

The Operational Boundary for External Debt – this is not an actual limit and actual borrowing can vary around this boundary during the year. It is based on the probable external debt during the course of the year.

No.	Prudential indicators For Prudence	TMS Limit 2017-18 £m	Actual 31-03-18 £m
5.	**Authorised limit for external debt -**		
	Borrowing	140	
	Other long term liabilities	30	
	Total	**170**	
6.	**Operational Boundary**		
	Borrowing	105	
	Other long term liabilities	25	
	Total	**130**	
	Borrowing		**96.87**
	Other long term liabilities		**21.02**
	Total		**117.89**

2.3 Prudential Indicators for Affordability

2.3.1 The **Ratio of Financing Costs to Net Revenue Stream** indicator demonstrates the trend in the cost of capital against the Total Revenue amount to be met from local taxpayers and the amount provided by the Welsh Government in the form of Revenue Support Grant. The estimates of capital financing costs include interest payable and receivable on treasury management activities and the MRP charged to the Comprehensive Income and Expenditure Statement. The revenue stream is the amount to be met from government grants and local taxpayers.

No.	Prudential Indicators for Affordability 2017-18	Estimate TMS 2017-18 %	Revised Projection 2017-18 TMS 2018-19 %	Actual 2017-18 %
7.	**Ratio of Financing Costs to Net Revenue Stream**	4.84	4.79	**4.72**

APPENDIX B

Credit Rating Equivalence Table

	Description	Fitch Long	Fitch Short	Moody's Long	Moody's Short	Standard & Poor's Long	Standard & Poor's Short
INVESTMENT GRADE	Extremely strong	AAA		Aaa		AAA	
	Very strong	AA+	F1+	Aa1		AA+	A-1+
		AA		Aa2	P-1	AA	
		AA-		Aa3		AA-	
	Strong	A+		A1		A+	
		A	F1	A2		A	A-1
		A-		A3		A-	A-2
	Adequate	BBB+	F2	Baa1	P-2	BBB+	
		BBB		Baa2		BBB	
		BBB-	F3	Baa3	P-3	BBB-	A-3
SPECULATIVE GRADE	Speculative	BB+		Ba1		BB+	
		BB		Ba2		BB	
		BB-	B	Ba3		BB-	B
	Very speculative	B+		B1		B+	
		B		B2		B	
		B-		B3	Not Prime (NP)	B-	
	Vulnerable	CCC+		Caa1		CCC+	
		CCC		Caa2		CCC	
		CCC-	C	Caa3		CCC-	C
		CC		Ca		CC	
		C				C	
	Defaulting	D	D	C		D	D