COUNCIL
26 SEPTEMBER 2019

TREASURY MANAGEMENT ANNUAL REPORT AND OUTTURN PRUDENTIAL INDICATORS 2018/19

Responsible Cabinet Member - Councillor Charles Johnson, Deputy Leader & Efficiency and Resources Portfolio

Responsible Director - Paul Wildsmith, Managing Director

SUMMARY REPORT

Purpose of the Report

1. This report provides important information regarding the regulation and management of the Council's borrowing, investments and cash-flow. It is a requirement of the Council's reporting procedures and covers treasury activity for 2018/19. The report also seeks approval of the Prudential Indicators results for 2018/19 in accordance with the Prudential Code.

Summary

2. The financial year 2018/19 presented similar circumstances to 2017/18 with regard to treasury management. However, as Members are aware due to the recent low returns for cash investments new ways to improve investment returns are continually being sought. It was agreed to look at alternative investment types to increase return. Cost of borrowing remained low throughout 2018/19 and the cost of shorter term borrowing is anticipated to remain low for a number of years in the future.

3. During 2018/19 the Council complied with its legislative and regulatory requirements. The borrowing need (Table 1) was only increased for capital purposes.

4. At 31st March 2019 the Council's external debt was £179.161m which is £19.000m more than the previous year, this increase relates to externalising debt which was in the past internal i.e. use of reserves as well as additional borrowing to fund the premium on the redemption of two of the Council's Lender Option Borrower Option (LOBO) loans. The average interest rate for borrowing was down from 3.84% in 2017/18 to 3.22% in 2018/19. This reduction in the average rate of interest is due to a new mix of maturity dates to take advantage of the lower cost of borrowing for short term debt. Investments totalled £55.849m at 31st March 2019 (£52.433m at 31st March 2018) earning interest of 0.69% on short term cash investments and 2.3% on Property Fund units net of costs.

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5. Financing costs have been reduced during the year and a saving of £0.661m has been achieved from the original MTFP. The majority of the savings relate to the increase in activity in the joint venture market as well as savings on debt repayments attributable to the redemption of the LOBO's.

Recommendation

6. It is recommended that:

   (a) The outturn 2018/19 Prudential Indicators within this report and those in **Appendix 1** be noted.

   (b) The Treasury Management Annual Report for 2018/19 be noted.

Reasons

7. The recommendations are supported by the following reasons:

   (a) In order to comply with the Prudential Code for Capital Finance in Local Authorities.

   (b) To inform members of the Performance of the Treasury Management function.

   (c) To comply with the requirements of the Local Government Act 2003.

Paul Wildsmith
Managing Director

Background Papers

(i) Accounting Records
(ii) Annual Investment Strategy 2018/19
(iii) Prudential Indicators and Treasury Management Strategy Report 2018/19

Peter Carrick: Extension 5401

S17 Crime and Disorder	This report has no implications for crime and disorder
Health and Well Being	There are no issues relating to health and wellbeing which this report needs to address
Carbon Impact	There are no issues relating to carbon impact
Diversity	There are no specific implications for diversity
Wards Affected	The proposals affect all wards
Groups Affected	The proposals do not affect any specific group
Budget and Policy Framework	The report does not change the Council's budget or Policy framework but needs to be considered by Council
Key Decision	This is not an Executive decision
Urgent Decision	This is not an Executive decision
One Darlington: Perfectly Placed	The proposals in the report support delivery of the Community Strategy through appropriate and effective deployment of the Councils Resources
Efficiency	The report outlines movements in the national economic outlook that have enabled officers to take advantage of different types of Investments and changing interest rates to benefit the Revenue MTFP.
Impact on Looked After Children and Care Leavers	Does this report impact on Looked After Children or Care Leavers

MAIN REPORT

Information and Analysis

8. This report summarises:

   (a) Capital expenditure and financing for 2018/19
   (b) The Council's underlying borrowing need
   (c) Treasury position at 31st March 2019
   (d) Prudential indicators and compliance issues
   (e) The economic background for 2018/19
   (f) A summary of the Treasury Management Strategy agreed for 2018/19
   (g) Treasury Management activity during 2018/19
   (h) Performance and risk benchmarking

9. Throughout this report a number of technical terms are used, a glossary of terms can be found at the end of this report.

The Council's Capital Expenditure and Financing 2018/19

10. The Council undertakes capital expenditure on long term assets, which is financed either,

    (a) immediately through capital receipts, capital grants, contributions and from revenue; or
    (b) by borrowing.

11. Part of the Council's treasury activities is to address this borrowing need, either through borrowing from external bodies, or utilising temporary cash resources within the Council. The wider treasury activities also include managing the Council's cash flow, its previous borrowing activities and the investment of surplus funds. These activities are structured to manage risk foremost and then optimise performance.

12. Capital Expenditure forms one of the prudential indicators that are used to regulate treasury activity. Table 1 shows total capital expenditure and how this was financed, compared with what was expected to be spent and how this would have been financed. Actual expenditure was £0.914m more than planned, partly due to increased activity in the Joint Venture market. However the mix of funding differs from that which was expected as some schemes progressed quicker than others. This impacted slightly on the borrowing needed to fund expenditure which was £1.995m higher than initially anticipated.

Table 1 – Capital Expenditure and Financing

	2017/18	2018/19		
	Outturn £m	Revised Estimate £m	Outturn £m	Variance £m
General Fund Capital Expenditure	24.797	18.507	21.298	2.791
HRA Capital Expenditure	15.634	12.370	9.376	(2.994)
Loans to Joint Ventures etc	0.000	5.000	6.117	1.117
Loan Facility to RSL's	0.000	0.000	0.000	0.000
Total Capital Expenditure	**40.431**	**35.877**	**36.791**	**0.914**
Resourced by:				
Capital Receipts GF	5.534	5.678	3.022	(2.656)
Capital receipts Housing	0.985	0.198	0.550	0.352
Capital Grants	13.349	7.863	9.336	1.473
Capital Contributions	1.716	0.000	4.076	4.076
Revenue Contributions - GF	0.000	1.600	0.000	(1.600)
Revenue (Housing)	13.424	12.172	9.446	(2.726)
Total Resources	**35.008**	**27.511**	**26.430**	**(1.081)**
Borrowing needed to finance expenditure	**5.423**	**8.366**	**10.361**	**1.995**

The Council's Underlying Borrowing Need

13. The Council's underlying need to borrow is called the Capital Financing Requirement (CFR). The figure is a gauge for the Council's debt position. It represents 2018/19 and prior years' net capital expenditure which has not yet been paid for by revenue or other resources.

14. The General Fund element of the CFR is usually reduced each year by a statutory charge to the revenue accounts called the Minimum Revenue Provision (MRP). The total CFR can also be reduced each year through a Voluntary Revenue Provision (VRP).

15. The Council's CFR for the year is shown in Table 2, and represents a key prudential indicator. The CFR outturn for 2018/19 is £207.348m which is £112.139m lower than approved because of the lower borrowing need than expected for 2018/19, mainly due to not requiring borrowing for loans to Registered Social Landlords (RSL's).

16. No MRP repayments were made on the General Fund debt in line with the report to Council on 23 February 2017.

Table 2 - Capital Financing Requirement

	2017/18	2018/19		
	Outturn £m	Approved Indicator £m	31 March Actual £m	Variance £m
Opening Balance	180.169	316.288	198.788	(117.500)
Add adjustment for the inclusion of leases on the balance sheet under IFRS	15.017	0.000	0.000	0.000
Add Capital Expenditure financed by borrowing	5.423	5.000	10.361	5.361
Less MRP/VRP General Fund	0.000	0.000	0.000	0.000
Less MRP/VRP Housing	(0.629)	(0.629)	(0.629)	(0.000)
Less MRP/VRP PFI	(1.192)	(1.172)	(1.172)	0.000
Closing balance	**198.788**	**319.487**	**207.348**	**(112.139)**

Treasury Position at 31 March 2019

17. Whilst the measure of the Council's underlying need to borrow is the CFR, the Assistant Director of Resources can manage the Council's actual borrowing position by:

    (a) borrowing to the CFR level; or
    (b) choosing to utilise some temporary cash flows instead of borrowing ("under borrowing"); or
    (c) borrowing for future increases in CFR (borrowing in advance of need, the "over borrowed" amount can be invested).

18. The financial reporting practice that the Council is required to follow (the Statement of Recommended Practice (SORP)), changed in 2007/08. Financial instruments (borrowing and investments etc.) must now be reported in the Statement of Accounts in accordance with national Financial Reporting Standards. The figures in this report are based on actual amounts borrowed and invested and so will differ from those in the Statement of Accounts which due to statutory requirements are shown at Fair Value.

19. The Council's total debt outstanding at 31 March 2019 was £179.161m. In addition to this, a liability of £12.653m relating to the PFI scheme and Finance Leases brings the total to £191.814m. The Council's revised CFR position was estimated to be £319.487m, which included £100.000m that related to possible loans to RSL's which were not realised in 2018/19. However, the actual out turn position was £207.348m. When comparing this to our actual borrowing of £191.814m this meant that the Council was "under borrowed" by £15.534m. This "under borrowed" amount was financed by internal borrowing which means that the amount that could have been invested externally was reduced to cover this. The reduced under borrowed position still has the dual effect of reducing costs to the MTFP because borrowing costs are generally greater than investment returns and it reduces counterparty risk by reducing our exposure to banks and other financial institutions.

20. The treasury position at the 31 March 2019, including investments compared with the previous year is shown in table 3 below.

Table 3 – Summary of Borrowing and Investments

Treasury Position	31 March 2018		31 March 2019	
	Principal £m	Average Rate %	Principal £m	Net annualised Average Rate %
General Debt - Fixed Rate Debt, Market and Public Works Loan Board (PWLB)	135.161	4.08%	154.161	3.52%
Property Fund Borrowing	25.000	1.17%	25.000	1.17%
Total Debt	**160.161**	**3.84%**	**179.161**	**3.22%**
Cashflow Investments up to 6 months	21.000	0.31%	25.850	0.69%
Capital Investments over 6 months	2.000	0.625%	-	-
Property Fund Investment -net of costs	29.433	2.20%	29.999	2.30%
Total Investments	**52.433**		**55.849**	
Net borrowing position	**107.728**		**123.312**	

Prudential Indicators and Compliance Issues

21. Some prudential indicators provide an overview while others are specific limits on treasury activity. These indicators are shown below:

22. **Gross Borrowing and the CFR –** in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2017/18) plus the estimates of any additional capital financing requirement for the current (2018/19) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allowed the Council some flexibility to borrow in advance of its immediate capital needs in 2018/19. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

Table 4 – Gross Borrowing Compared with CFR

	31 March 2018 Actual £m	31 March 2019 Approved Indicator £m	31 March 2019 Actual £m
Gross Borrowing Position	**160.161**	**288.000**	**179.161**
PFI and Finance Lease Liability	**13.825**	**12.653**	**12.653**
CFR Excluding PFI & leases	**184.963**	**306.834**	**194.695**
CFR	**198.788**	**319.487**	**207.348**

23. **The Authorised Limit –** The Authorised Limit is the "Affordable Borrowing Limit" required by section 3 of the Local Government Act 2003. The Council does not have power to borrow above this level.

24. **The Operational Boundary –** The Operational Boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the Boundary are both acceptable, subject to the Authorised Limit not being breached.

25. **Actual financing costs as a proportion of net revenue expenditure -** This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue expenditure. The actual for this indicator has reduced due to nil provision of MRP for the General Fund and other savings in the Financing Costs budget, but has risen from the previous year due to a reduction in the Councils overall budget.

Table 5 – Key Prudential Indicators

	Actual 2017/18 £m	Original Approved Limits 2018/19 £m	Revised Approved Limits 2018/19 £m	Actual Total Liabilities Borrowing + PFI/ leases 2018/19 Maximum £m
Approved Indicator – Authorised Limit	**173.986**	**316.736**	**315.686**	**191.814**
Approved Indicator – Operational Boundary	**173.986**	**301.653**	**300.653**	**191.814**
Financing costs as a percentage of net revenue expenditure	**4.00%**	**4.59%**	**3.96%**	**4.07%**

26. At 31 March 2019 the total liabilities were £191.814m which is below both the approved Authorised Limit and the approved Operational Boundary. The Operational Boundary is the point at which we expect borrowing to be, but it can be lower or higher. Borrowing cannot exceed the Authorised Limit.

27. A further four prudential indicators are detailed in **Appendix 1**.

Economic Background for 2018/19

28. A summary of the general economic conditions that have prevailed through 2018/19 provided by Link Asset Services, the Council's treasury management advisors is attached at **Appendix 2.**

Summary of the Treasury Management Strategy agreed for 2018/19

29. The revised Prudential Indicators anticipated that during 2018/19 the Council would need to borrow £108.366m to finance part of its capital programme including £100.000M of loans to RSL's.

30. The Annual Investment Strategy stated that the use of specified (usually less than 1 year) and non-specified (usually more than 1 year) investments would be carefully balanced to ensure that the Council has appropriate liquidity for its operational needs. In the normal course of the Council's business it is expected that both specified and non-specified investments will be utilised for the control of liquidity as both categories allow for short term investments.

31. Longer term instruments (greater than one year from inception to repayment) will only be used where the Council's liquidity requirements are safeguarded. An estimate of long term investments (over 1 year) were included in the report on the Prudential Indicators update these were as follows £50m for 2018/19 and £50m for 2019/20. Three investments of up to £10m each were made in 3 Property Funds during July, August and December 2017. No other investments of over 1 year duration have been made during 2018/19.

Treasury Management Activity during 2018/19

Debt Position

32. **Borrowing –** this increased during 2018/19 by £19.000m in total

	PWLB			Market Loans (incl. other Local Authorities			Total
	Amount £m	Length of Loan	Interest Rate	Amount £m	Length of Loan	Interest Rate	£m
New Loans taken							
	5.000	5 years	1.82%	4.000	1 year	1.00%	
	5.000	42 years	2.47%	5.000	2 year	1.45%	
	5.000	43 years	2.46%	5.000	1 year	1.10%	
	5.000	44 years	2.46%				
	6.000	45 years	2.46%				
	6.250	46 years	2.45%				46.250
Loans Repaid							
	-13.750	42 years	7.00%				
	-13.500	41 years	7.00%				-27.250
Total New Borrowing	5.000			14.000			19.000

33. The new borrowing of £19.000m was taken for various lengths of time at various interest rates as shown above.

34. **Rescheduling –** As Members are aware the Council has held a number of Lender Option Borrower Option loans (LOBO's) since 2006, two of which were classified as 'Inverse LOBO's whereby the interest rate paid was linked to the prevailing '10 year swap rate' which meant that the higher the interest rate (linked to base rate) the less the Council paid in interest payments and vice versa.

35. An opportunity to redeem the two inverse LOBO's arose in December 2018 whereby even with the associated cost of the premium for early settlement the savings to the Council in cash terms are £20.807m over the remaining 42 years of the loan and £10.611m at NPV discounted rates.

36. **Summary of Debt Transactions –**The consolidated rate of interest decreased from 3.84% to 3.22% due to the above transactions.

Investment Position

37. **Investment Policy –** the Council's investment policy for 2018/19 is governed by the DCLG Guidance which has been implemented in the annual investment strategy for 2018/19 approved by Council on 22 February 2018.

38. The investment activity during the year conformed to the approved Strategy and the Council had no liquidity difficulties.

39. Investments held by the Council consist of temporary surplus balances, capital receipts and other funds.

Table 6 Temporary Surplus Cash Balances up to 6 months

	Original Budget 2018/19	**Revised Budget 2018/19**	**Actual 2018/19**
Daily average level of Investments	**£14.400m**	**£14.285m**	**£20.190m**
Average Rate of Return on Investment	**0.25%**	**0.50%**	**0.68%**
Interest Earned	**£36,000**	**£70,000**	**£136,000**

Table 7a – Longer Term 6 months to 5 years Cash

	Original Budget 2018/19	**Revised Budget 2018/19**	**Actual 2018/19**
Daily average level of Investments	**£8.000m**	**£8.000m**	**£7.720m**
Average Rate of Return on Investment	**0.35%**	**0.60%**	**0.71%**
Interest Earned	**£28,000**	**£48,000**	**£55,000**

Table 7b – Longer Term 6 months to 5 years - Property Funds

	Original Budget 2018/19	**Revised Budget 2018/19**	**Actual 2018/19**
Daily average level of Investments	**£29.433m**	**£29.933m**	**£29.999m**
Average Rate of Return on Investment (gross)	**3.81%**	**3.57%**	**3.54%**
Interest Earned (Gross)	**£1,122,000**	**£1,068,000**	**£1,062,000**

Performance and Risk Benchmarking

40. A regulatory development is the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance and these are shown in **Table 10**. Discrete security and liquidity benchmarks are relatively new requirements to the member reporting. These were first set in the Treasury Strategy report of the 25th February 2010.

41. The following reports the current position against the benchmarks originally approved.

42. Security – The Council's maximum security risk benchmarks for the current portfolio of investments, when compared to historic default tables was set as follows:

    0.077% historic risk of default when compared to the whole portfolio

43. **Table 8** shows that there has been a reduction in the historic levels of default over the year. This is mainly due to some longer term investments actually being made for shorter terms i.e. up to six months rather than 1 year as these investments were better value than longer term investments and were also a better fit with how the council was expecting to utilise investments. It also shows more emphasis being placed on counterparties with a higher credit rating.

44. The investment portfolio was maintained within this overall benchmark during this year as shown in **Table 8**.

Table 8

Maximum	Benchmark 2018/19	Actual June 2018	Actual October 2018	Actual January 2019	Actual March 2019
Year 1	0.077%	0.009%	0.005%	0.001%	0.001%

45. The counterparties that we use are all high rated therefore our actual risk of default based on the ratings attached to counterparties is virtually nil.

46. Liquidity – In respect of this area the Council set liquidity facilities/benchmark to maintain

    (a) Bank Overdraft £0.100M
    (b) Liquid short term deposits of at least £3.000M available within a weeks' notice.
    (c) Weighted Average Life benchmark is expected to be 146 days with a maximum of 1year.

47. Liquidity arrangements have been adequate for the year to date as shown in Table 9.

Table 9

	Benchmark	Actual June 2018	Actual October 2018	Actual January 2019	Actual March 2019
Weighted Average life	**146days to 1 years**	**80 days**	**36 days**	**7 days**	**6 days**

48. This benchmark includes fixed term investments are for up to 1 year with cash flow monies being invested in Money Market funds which can be accessed immediately.

49. Yield - In respect of this area performance indicators relating to interest rates for borrowing and investments were set with reference to comparative interest rates. For borrowing, the indicator is the average rate paid during the year compared with

the previous year. Investment rates are compared with a representative set of comparative rates.

Table 10 – Performance Compared With Indicators

Borrowing	Average overall rate paid compared to previous years	**2017/18 3.84%**	**2018/19 3.22%**
Investments		**DBC 2017/18**	**DBC 2018/19**
Short term	Cash flow investment rate returned against comparative average rate	0.31%	**0.68%**
Long term	Capital investment rate returned against comparative average rates	0.53%	**0.71%**
Comparative rates used to compare DBC performance: -		**Short Term Investments**	**Long Term Investments**
Comparative Rates			
Overnight Bid Rate Overnight		0.50%	-
London Interbank Bid Rate 7 day		0.51%	-
London Interbank Bid Rate 1 month		0.54%	-
London Interbank Bid rate 3 months		0.68%	-
London Interbank Bid rate 6 months		-	0.79%
London Interbank Bid rate 12 months		-	0.94%
Average External Comparators		**0.56%**	**0.87%**

50. As can be seen from the table, the actual investment rate achieved for short term investments exceeds the average of comparative rates whilst the longer term comparator is not exceeded due to the comparator being at the end of March 2019 whereas the actual indicator was for the beginning of the year when rates were lower.

Risk

51. The Council's treasury management activities are regulated by a variety of professional codes, statutes and guidance:-

(a) The Local Government Act 2003(the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity.

(b) The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions were made in 2017/18).

(c) Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act.

(d) The SI requires the Council to undertake any borrowing activity with regard to the CIFPA Prudential Code for Capital Finance in Local Authorities.

(e) The SI also requires the Council to operate the overall treasury function with regard to the CIPFA code of Practice for Treasury Management in Public Services.

(f) Under the Act the Department for Communities and Local Government has issued Investment Guidance to structure and regulate the Council's investment activities.

(g) Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices. Guidance on Minimum Revenue Provision was issued under this section on 8 November 2007.

52. The Councils Treasury Management function has complied with all of the relevant statutory and regulatory requirements, which limit the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable and its treasury practices demonstrate a low risk approach.

53. Officers of the Council are aware of the risks of passive management of the treasury portfolio and, with the support of Capita Asset Services, the Council's advisers, have proactively managed the debt and investments over the year.

Treasury Management Budget

54. There are three main elements within the Treasury Management Budget :-

(a) Long Term capital investments including Property Funds which earns interest, this comprises of the Council's revenue and capital balances, unused capital receipts, reserves and provisions.

(b) Cash flow interest earned – since becoming a unitary council in 1997, the authority has consistently had positive cash flow. Unlike long term capital investments it does not represent any particular sum but it is the consequence of many different influences such as receipts of grants, the relationship between debtors and creditors, cashing of cheques and payments to suppliers.

(c) Debt servicing costs – This is the principal and interest costs on the Council's long term debt to finance the capital programme.

Table 11 Changes to the Treasury Management Budget 2018/19

	£m	**£m**
Original Treasury Management Budget		**0.915**
Debt		
Less reduced interest payable on debt	**(0.249)**	
Less further savings on MRP	**(0.131)**	

	£m	£m
Add additional annual premium on rescheduled debt	**0.077**	**(0.303)**
Investments		
Less increased investment income including property funds/Joint Ventures etc		**(0.465)**
Other Costs		
Add increased brokerage charges (including LOBO redemption)		**0.107**
Outturn Treasury Management Budget 2018/19		**0.254**

55. The majority of the savings relate to the inclusion and purchase of Property Fund units in the investment portfolio, with the return reduced due to additional interest payments on debt and additional brokerage fees.

Conclusion

56. The Council's treasury management activity during 2018/19 has been carried out in accordance with Council Policy and within legal limits. Financing costs have been reduced during the year and a saving of £0.661m achieved from the original MTFP.

Outcome of Consultation

57. No formal consultation has been undertaken regarding this report.

APPENDIX 1

Additional Prudential Indicators not reported in the body of the report

		2017/18 Actual	2018/19 Approved Indicator	2018/19 Outturn
1	**Upper limits on fixed interest rates (*against maximum position*)**	**83%**	**100%**	**79%**
2	**Upper limits on variable interest rates (*against maximum position*)**	**17%**	**40%**	**21%**
3	**Maturity structure of fixed rate borrowing (*against maximum position*)**			
	Under 12 months	**17%**	**25%**	**21%**
	12 months to 2 years	**3%**	**40%**	**6%**
	2 years to 5 years	**10%**	**60%**	**11%**
	5 years to 10 years	**5%**	**80%**	**7%**
	10 years and above	**65%**	**100%**	**55%**
4	**Maximum Principal funds invested greater than 364 days**	**£30m**	**£50m**	**£50m**

APPENDIX 2

The Economy and Interest Rates

1. **UK.** After weak **economic growth** of only 0.2% in quarter one of 2018, growth picked up to 0.4% in quarter 2 and to a particularly strong 0.7% in quarter 3, before cooling off to 0.2% in the final quarter. Given all the uncertainties over Brexit, this weak growth in the final quarter was as to be expected. However, some recovery in the rate of growth is expected going forward. The annual growth in Q4 came in at 1.4% y/y confirming that the UK was the third fastest growing country in the G7 in quarter 4.
2. 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 the uncertainties over Brexit clear. If there were a disorderly exit, it is likely that Bank Rate would be cut to support growth. Nevertheless, the MPC has been having increasing concerns over the trend in **wage inflation** which peaked at a new post financial crisis high of 3.5%, (excluding bonuses), in the three months to December before falling only marginally to 3.4% in the three months to January. British employers ramped up their hiring at the fastest pace in more than three years in the three months to January as the country's labour market defied the broader weakness in the overall economy as Brexit approached. The number of people in work surged by 222,000, helping to push down the unemployment rate to 3.9 percent, its lowest rate since 1975. Correspondingly, the total level of vacancies has risen to new highs.
3. As for **CPI inflation** itself, this has been on a falling trend since peaking at 3.1% in November 2017, reaching a new low of 1.8% in January 2019 before rising marginally to 1.9% in February. However, in the February 2019 Bank of England Inflation Report, the latest forecast for inflation over both the two and three year time horizons remained marginally above the MPC's target of 2%.
4. The rise in wage inflation and 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 1.5%, i.e. a real terms 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.
5. **Brexit.** The Conservative minority government has so far, (8.4.19), been unable to muster a majority in the Commons over its Brexit deal. The EU has set a deadline of April 12 for the House of Commons to propose what form of Brexit it would support. If another form of Brexit, other than the proposed deal, does get a majority by April 12, then it is likely there will need to be a long delay to Brexit to allow time for negotiations with the EU. It appears unlikely that there would be a Commons majority which would support a disorderly Brexit or revoking article 50, (cancelling Brexit). There would also need to be a long delay if there is no majority for any form of Brexit. If that were to happen, then it increases the chances of a general election in 2019; this could result in a potential loosening of monetary policy and therefore medium to longer dated gilt yields could rise on the expectation of a weak pound and concerns around inflation picking up.

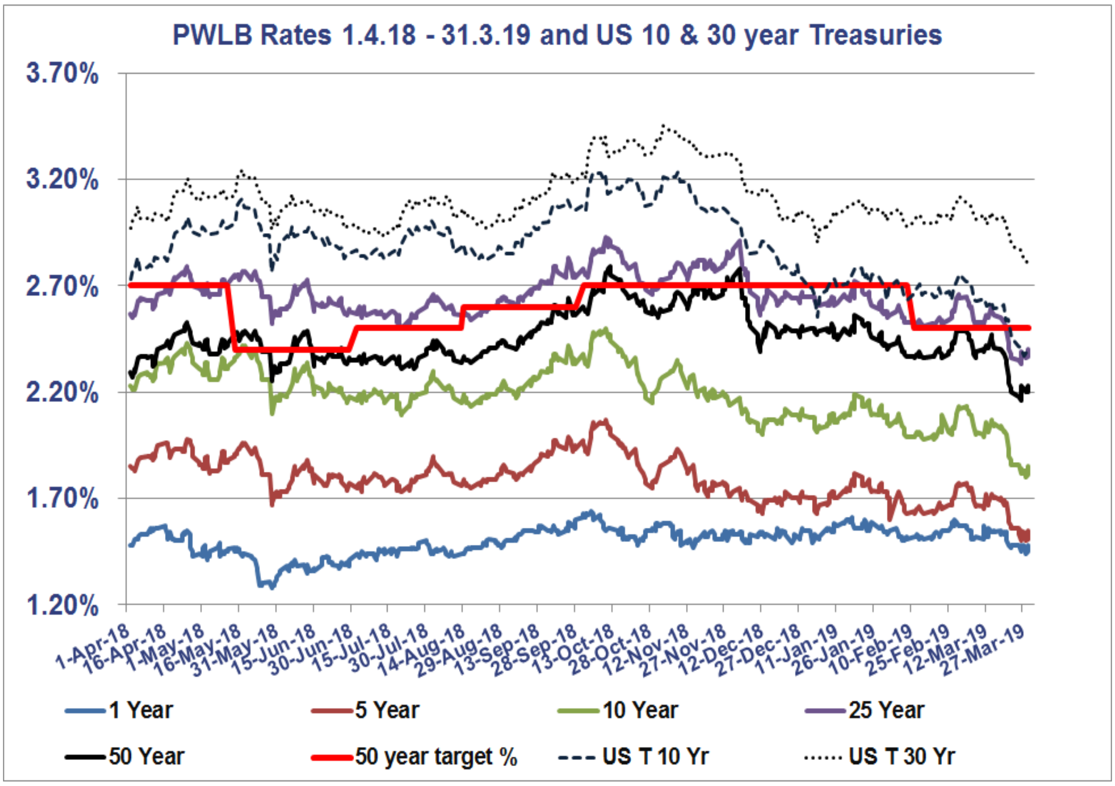
6. **USA.** President Trump's massive easing of fiscal policy in 2018 fuelled a (temporary) boost in consumption in 2018 which generated an upturn in the strong rate of growth; this rose from 2.2%, (annualised rate) in quarter 1 of 2018 to 4.2% in quarter 2, 3.5% in quarter 3 and then back to 2.2% in quarter 4. The annual rate came in at 2.9% for 2018, just below President Trump's aim for 3% growth. The strong growth in employment numbers has fed through to an upturn in wage inflation which hit 3.4% in February, a decade high point. However, CPI inflation overall fell to 1.5% in February, a two and a half year low, and looks to be likely to stay around that number in 2019 i.e. below the Fed's target of 2%. The Fed increased rates another 0.25% in December to between 2.25% and 2.50%, this being the fourth increase in 2018 and the ninth in the upward swing cycle. However, the Fed now appears to be edging towards a change of direction and admitting there may be a need to switch to taking action to cut rates over the next two years. Financial markets are now predicting two cuts of 25 bps by the end of 2020.

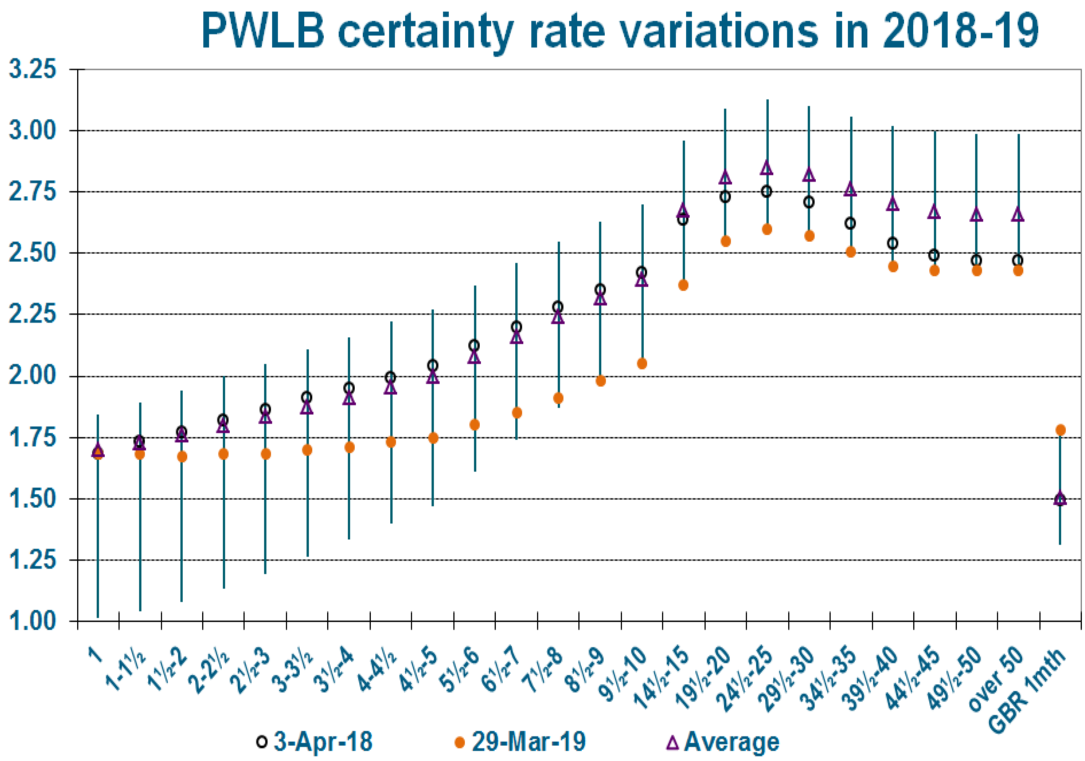
7. **EUROZONE.** The European Central Bank (ECB) provided massive monetary stimulus in 2016 and 2017 to encourage growth in the EZ and that produced strong annual growth in 2017 of 2.3%. However, since then the ECB has been reducing its monetary stimulus measures and growth has been weakening - to 0.4% in quarters 1 and 2 of 2018, and then slowed further to 0.2% in quarters 3 and 4; it is likely to be only 0.1 - 0.2% in quarter 1 of 2019. The annual rate of growth for 2018 was 1.8% but is expected to fall to possibly around half that rate in 2019. The ECB completely ended its programme of quantitative easing purchases of debt in December 2018, which means that the central banks in the US, UK and EU have all ended the phase of post financial crisis expansion of liquidity supporting world financial markets by purchases of debt. However, the downturn in growth, together with inflation falling well under the upper limit of its target range of 0 to 2%, (but it aims to keep it near to 2%), prompted the ECB to take new measures to stimulate growth. With its refinancing rate already at 0.0% and the deposit rate at -0.4%, it has probably reached the limit of cutting rates. At its March 2019 meeting it said that it expects to leave interest rates at their present levels "at least through the end of 2019", but that is of little help to boosting growth in the near term. Consequently, it also announced a third round of TLTROs; this provides banks with cheap borrowing every three months from September 2019 until March 2021 which means that, although they will have only a two-year maturity, the Bank is making funds available until 2023, two years later than under its previous policy. As with the last round, the new TLTROs will include an incentive to encourage bank lending, and they will be capped at 30% of a bank's eligible loans.

8. **CHINA.** Economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems.

9. **JAPAN** - has been struggling to stimulate consistent significant GDP growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

10. **WORLD GROWTH.** Equity markets are currently concerned about the synchronised general weakening of growth in the major economies of the world: they fear there could even be a recession looming up in the US, though this fear is probably overdone.


PWLB Rates 1.4.18 - 31.3.19 and US 10 & 30 year Treasuries
3.70%
3.20%
2.70%
2.20%
1.70%
1.20%
1-Apr-18
16-Apr-18
1-May-18
16-May-18
31-May-18
15-Jun-18
30-Jun-18
15-Jul-18
30-Jul-18
14-Aug-18
29-Aug-18
13-Sep-18
28-Sep-18
13-Oct-18
28-Oct-18
12-Nov-18
27-Nov-18
12-Dec-18
27-Dec-18
11-Jan-19
26-Jan-19
10-Feb-19
25-Feb-19
12-Mar-19
27-Mar-19
1 Year
5 Year
10 Year
25 Year
50 Year
50 year target %
US T 10 Yr
US T 30 Yr


PWLB certainty rate variations in 2018-19
3.25
3.00
2.75
2.50
2.25
2.00
1.75
1.50
1.25
1.00
1
1-1½
1½-2
2-2½
2½-3
3-3½
3½-4
4-4½
4½-5
5½-6
6½-7
7½-8
8½-9
9½-10
14½-15
19½-20
24½-25
29½-30
34½-35
39½-40
44½-45
49½-50
over 50
GBR 1mth
3-Apr-18
29-Mar-19
Average

	1 Year	5 Year	10 Year	25 Year	50 Year
02/04/2018	1.48%	1.85%	2.23%	2.57%	2.29%
29/03/2019	1.48%	1.55%	1.85%	2.40%	2.23%
Low	1.28%	1.50%	1.80%	2.33%	2.16%
Date	29/05/2018	26/03/2019	28/03/2019	26/03/2019	26/03/2019
High	1.64%	2.07%	2.50%	2.93%	2.79%
Date	04/10/2018	10/10/2018	10/10/2018	10/10/2018	12/10/2018
Average	1.50%	1.80%	2.20%	2.66%	2.47%

Since PWLB rates peaked during October 2018, most PWLB rates have been on a general downward trend, though longer term rates did spike upwards again during December, and, (apart from the 1 year rate), reached lows for the year at the end of March. There was a significant level of correlation between movements in US Treasury yields and UK gilt yields -which determine PWLB rates. The Fed in America increased the Fed Rate four times in 2018, making nine increases in all in this cycle, to reach 2.25% – 2.50% in December. However, it had been giving forward guidance that rates could go up to nearly 3.50%. These rate increases and guidance caused Treasury yields to also move up. However financial markets considered by December 2018, that the Fed had gone too far, and discounted its expectations of further increases. Since then, the Fed has also come round to the view that there are probably going to be no more increases in this cycle. The issue now is how many cuts in the Fed Rate there will be and how soon, in order to support economic growth in the US. But weak growth now also looks to be the outlook for China and the EU so this will mean that world growth as a whole will be weak. Treasury yields have therefore fallen sharply during 2019 and gilt yields / PWLB rates have also fallen

Glossary of Terms

Capital Financing Requirement (CFR)	This is the Councils underlying need to borrow which can be traced back to the Councils Balance Sheet and the value of the Councils assets which have yet to be paid for.
Minimum Revenue Provision (MRP)	Monies set aside from the revenue budget to repay accumulated debt.
Call	Investments that can be returned without a period of notice
Counterparty	Institutions, Banks etc. that with make investments or take out loans with.
Specified Investments	Investments in Banks and Building Societies with a high credit rating for periods of less than 1 year
Non-Specified Investments	Investments in un rated Building Societies and any investments in Banks and Building Societies for more than 1 year.
Operational Liquidity	Working Cash flow
Authorised Limit	Maximum amount of borrowing that could be taken in total.
Operational Boundary	The expected amount of borrowing assumed in total.
PWLB	Public Works Loan Board. The Governments lending body to Local Authorities
Discount	Amount payable by the PWLB when loans are repaid if the current loan rate is less than the rate borne by the original debt
Yield Curve	Is a graph that shows the relationship between the interest rate paid and length of time to repayment of a loan.
Gilts	Government Borrowing Bonds
Spreads	The difference between the highest rate of interest and the lowest rate of interest earned/charged on any one particular maturity period i.e. 1 year, 2 year 5 year etc.
LIBID	London Interbank Bid Rate. The average rate at which a bank is willing to borrow from another bank.
LIBOR	London Interbank Offer Rate. The average rate at which a bank is willing to lend to another bank. LIBOR is always higher than the corresponding bid rate and the difference between the two rates is known as the spread.