

REQUEST FOR DMPC DECISION – PCD 309

Title: Treasury Management – 2017/18 Mid-Year Report

Executive Summary:

The Treasury Management strategy 2017/18 sets out planned capital spending and how MOPAC will manage its borrowings and investments during this financial year. The GLA Treasury Management team provide the operational support for this function and through the Group Investment Syndicate (GIS) manages all MOPAC investments, to generate financial and risk reduction benefits.

To 30 September 2017 interest income for the first half year was £1m, and is ahead of expected half year budget of £0.65m. At 0.44%, the weighted average yield exceeds the benchmark by 0.26%. Debt management costs for the period are £9.4m, and are forecast to be below the budget of £20.2m at year end. There was no new borrowing in the period.

All investment and borrowing activity during 1 April 2017 and to 30 September 2017 was undertaken within the guidelines and objectives set out in the relevant policy and investment and borrowing strategies.

Recommendation:

That the DMPC notes the activity and performance on the Treasury Management function for the first half year 2017/18

Deputy Mayor for Policing and Crime

I confirm I have considered whether or not I have any personal or prejudicial interest in this matter and take the proposed decision in compliance with the Code of Conduct. Any such interests are recorded below.

The above request has my approval.

Signature

Sybil Winder

Date

18/01/18

PART I - NON-CONFIDENTIAL FACTS AND ADVICE TO THE DMPC

Decision required – supporting report

1. Introduction and background

- 1.1. MOPAC approved the 2017/18 Treasury Management Strategy in March 2017, PCD 179. This paper fulfils the requirement for reporting of mid-year performance to the DMPC.

2. Issues for consideration

Borrowing

- 2.1. There has been no new long term borrowing in the first six months of 2017-18, and due to loan repayments the total borrowing has reduced from £159m to £150m – a reduction of £9m. Borrowing costs for the first 6 months was £9.4m, and are forecast to be £18.8m against a budget of £20.2m.

Investment

- 2.2. The weighted average yield on investments was 0.44%, compared with the LIBID 3 month benchmark of 0.18%, generating income of £1m. The annual budget for interest receivable is £1.3m, and is forecast to be exceeded due to higher than expected balances and increasing deposit rates.

Prudential Indicators and Treasury Management Limits

- 2.3. The attached appendix sets out the detail of performance against the prudential indicators and treasury management limits. All transactions undertaken during the year met the criteria for lending to institutions and activity has been within the Prudential Code indicators set out in the TM Strategy 2017-18.

Forthcoming issues

- 2.4. The Chartered Institute of Public Finance and Accountancy (CIPFA) recently consulted on prudential indicators and the treasury management code of practice. MOPAC were engaged through the Police & Crime Commissioners Treasurers Society. The revised code and indicators are expected to be for application in 2018/19.
- 2.5. The draft capital programme included in the budget submission envisages new borrowing to meet the further investment proposed. The revenue costs of the additional borrowing are included in the revenue budget. MOPAC currently maintains an under-borrowed position, such that the capital financing requirement has not been fully funded with loan debt but by using the cash supporting MOPAC's reserves, balances and cashflow. The delivery of the future capital programme, budgeted revenue savings, use of reserves and the phasing of new asset disposals will impact the cashflow, and will be kept under review. Further borrowing to address the under-borrowed position may be required, and will be considered as part of the Treasury Management strategy 2018/19.

3. Financial Comments

- 3.1. This is a financial report and the details are set out in the body of the report.

4. Legal Comments

- 4.1. Under Section 1 of the Local Government Act 2003, MOPAC as local authority defined under s23 of that Act, may borrow money for any purpose relevant to its functions under any enactment, or for the purpose of the prudent management of its financial affairs.
- 4.2. The Mayor is required under s3 of the Local Government Act 2003 to determine how much money the GLA and each functional body (which includes MOPAC) can afford to borrow. In complying with this duty, Regulation 2 of the Local Authorities (Capital Finance and Accounting)(England) Regulations 2003 requires the Mayor to have regard to the Prudential Code for Capital Finance in Local Authorities when determining how much MOPAC can afford.
- 4.3. MOPAC's scheme of delegation provides that the Chief Finance Officer, as the s127 officer, is responsible for the proper administration of the MOPAC's financial affairs.
- 4.4. An investment strategy statement must be completed as part of risk management and good governance. The report is submitted in compliance with TMSS and DCLG requirements in this regard.

5. Equality Comments

- 5.1. There are no equality or diversity implications arising from this report.

6. Background/supporting papers

GLA Report Appendix 1

Public access to information

Information in this form (Part 1) is subject to the Freedom of Information Act 2000 (FOIA) and will be made available on the MOPAC website following approval.

If immediate publication risks compromising the implementation of the decision it can be deferred until a specific date. Deferral periods should be kept to the shortest length strictly necessary.

Part 1 Deferral:

Is the publication of Part 1 of this approval to be deferred? No

If yes, for what reason:

Until what date:

Part 2 Confidentiality: Only the facts or advice considered as likely to be exempt from disclosure under the FOIA should be in the separate Part 2 form, together with the legal rationale for non-publication.

Is there a **Part 2** form – No

ORIGINATING OFFICER DECLARATION:

	<i>Tick to confirm statement (✓)</i>
Head of Unit: The Chief Finance Officer has reviewed the request and is satisfied it is correct and consistent with the MOPAC's plans and priorities.	✓
Legal Advice: Legal advice is not required	✓
Financial Advice: The Strategic Finance and Resource Management Team has been consulted on this proposal.	✓
Equalities Advice: Equality and diversity issues are covered in the body of the report.	✓

OFFICER APPROVAL**Chief Executive**

I have been consulted about the proposal and confirm that financial, legal and equalities advice has been taken into account in the preparation of this report. I am satisfied that this is an appropriate request to be submitted to the Deputy Mayor for Policing and Crime.

Signature R. Lawrence

Date 09/01/18

GREATER LONDON AUTHORITY

GROUP TREASURY

MOPAC Treasury Management Mid-Year Review for 2017-18

Executive Summary:

This report is submitted in accordance with a requirement under the Treasury Management in the Public Services Code of Practice (The Code), issued by the Chartered Institute of Public Finance and Accountancy (CIPFA), which requires the submission of a mid-year report on the activities of MOPAC's treasury management operation.

Treasury activity has seen MOPAC's investments outperform its investment benchmark by 0.26% over the six-month period ending 30 September 2017. Invested balances at 30 September 2017 were £468.80m.

MOPAC's borrowing levels have reduced from £159.46m at 31 March 2017 to £150.24m at 30 September 2017.

All Treasury activity has been within the boundaries and levels set by MOPAC and set out in the 2017/18 Treasury Management Strategy.

Recommendation:

That the following is noted:

- The 2017/18 Treasury mid-year performance against the 2017/18 Treasury Management Strategy Statement and forecasts.

Introduction/Background

- 1 This report provides detail of all investment and borrowing activities for the period from 1 April 2017 to 30 September 2017 and highlights relevant issues currently under consideration by officers. It provides a comparison of the closing investment and debt positions as at 30 September 2017 with the 17/18 full year budget and a revised 17/18 full year forecast, where relevant.
- 2 Under the treasury management shared service arrangement with the GLA, GLA group treasury officers carry out MOPAC's day to day treasury management function, managing its investments and borrowing activities. MOPAC/MPS officers provide the GLA with details of MOPAC's daily cash flow requirements and monies are only transferred between GLA and MOPAC as and when required to match MOPAC need. This way, surplus funds over and above daily need are continuously held with the Group Investment Syndicate (GIS), the GLA managed vehicle used to maximise liquidity and investment return.
- 3 The 17/18 GIS Investment Strategy was approved by MOPAC on 30 March 2017.

Compliance with the 2017/18 Treasury Management Strategy Statement

- 4 The GLA's Chief Investment Officer confirms that, throughout the period, all treasury activities have been conducted within the parameters of the 2017/18 Treasury Management Strategy Statement (TMSS), alongside best practice suggested by the Chartered Institute of Public Finance and Accountancy (CIPFA) and Central Government.

Economic Update and Interest Rates

- 5 After the UK economy surprised on the upside with strong growth in 2016, growth in 2017 has been disappointingly weak; quarter 1 came in at only +0.3% (+1.7% y/y) and quarter 2 was +0.3% (+1.5% y/y) which meant that growth in the first half of 2017 was the slowest for the first half of any year since 2012. The main reason for this has been the sharp increase in inflation, caused by the devaluation of sterling after the referendum, feeding increases in the cost of imports into the economy. This has caused, in turn, a reduction in consumer disposable income and spending power and so the services sector of the economy, accounting for around 75% of GDP, has seen weak growth as consumers cut back on their expenditure. However, more recently there have been encouraging statistics from the manufacturing sector which is seeing strong growth, particularly as a result of increased demand for exports. It has helped that growth in the EU, our main trading partner, has improved significantly over the last year. However, this sector only accounts for around 11% of GDP so expansion in this sector will have a much more muted effect on the average total GDP growth figure for the UK economy as a whole.
- 6 The Monetary Policy Committee (MPC) meeting of 14 September 2017 surprised markets and forecasters by suddenly switching to a much more aggressive tone in terms of its words around warning that Bank Rate will need to rise. The MPC duly delivered on those words in November by a vote of 7-2 to remove the post EU referendum emergency monetary stimulus implemented in August 2016 by reversing the cut in Bank Rate at that time from 0.5% to 0.25%.
- 7 The Bank of England Inflation Reports during 2017 have flagged up that they expected CPI inflation to peak at 3.2% in 2017, before falling back to near to its target rate of 2% in two years time.

- 8 The MPC also gave forward guidance that they expected to increase Bank Rate only twice more in the next three years to reach 1.0% by 2020. This is, therefore, not quite the 'one and done' scenario but is, nevertheless, a very relaxed rate of increase prediction in Bank Rate in line with previous statements that Bank Rate would only go up very gradually and to a limited extent. While there is so much uncertainty around the Brexit negotiations, consumer confidence, and business confidence to spend on investing, it is far too early to be confident about how the next two years will pan out.
- 9 The MOPAC's and GIS treasury advisor, Link Asset Services, has provided the following forecast as at 7 November:

	NOW	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20
BANK RATE	0.50	0.50	0.50	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00
3 month LIBID	0.40	0.40	0.40	0.40	0.40	0.60	0.60	0.60	0.70	0.90	0.90
6 month LIBID	0.45	0.50	0.50	0.50	0.60	0.80	0.80	0.80	0.90	1.00	1.00
12 month LIBID	0.65	0.70	0.80	0.80	0.90	1.00	1.00	1.10	1.10	1.30	1.30
5 yr PWLB	1.50	1.50	1.60	1.60	1.70	1.80	1.80	1.90	1.90	2.00	2.10
10 yr PWLB	2.10	2.10	2.20	2.30	2.40	2.40	2.50	2.60	2.60	2.70	2.70
25 yr PWLB	2.70	2.80	2.90	3.00	3.00	3.10	3.10	3.20	3.20	3.30	3.40
50 yr PWLB	2.40	2.50	2.60	2.70	2.80	2.90	2.90	3.00	3.00	3.10	3.20

- 10 The overall balance of risks to economic recovery in the UK is currently to the downside but huge variables over the coming few years include just what final form Brexit will take, when finally agreed with the EU, and when.
- 11 Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:
- Bank of England monetary policy takes action too quickly over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
 - Geopolitical risks, especially North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.
 - A resurgence of the Eurozone sovereign debt crisis, possibly Italy, due to its high level of government debt, low rate of economic growth and vulnerable banking system.
 - Weak capitalisation of some European banks.
 - The result of the October 2017 Austrian general election is likely to result in a strongly anti-immigrant coalition government. In addition, the new Czech prime minister is expected to be Andrej Babis who is strongly against EU migrant quotas and refugee policies. Both developments could provide major impetus to other, particularly former Communist bloc countries, to coalesce to create a major block to progress on EU integration and centralisation of EU policy. This, in turn, could spill over into impacting the Euro, EU financial policy and financial markets.
 - Rising protectionism under President Trump.
 - A sharp Chinese downturn and its impact on emerging market countries.

12 The potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- The Bank of England is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflation pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.
- UK inflation returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.
- The Fed causing a sudden shock in financial markets through misjudging the pace and strength of increases in its Fed. Funds Rate and in the pace and strength of reversal of QE, which then leads to a fundamental reassessment by investors of the relative risks of holding bonds, as opposed to equities. This could lead to a major flight from bonds to equities and a sharp increase in bond yields in the US, which could then spill over into impacting bond yields around the world.

Current Treasury Management Position

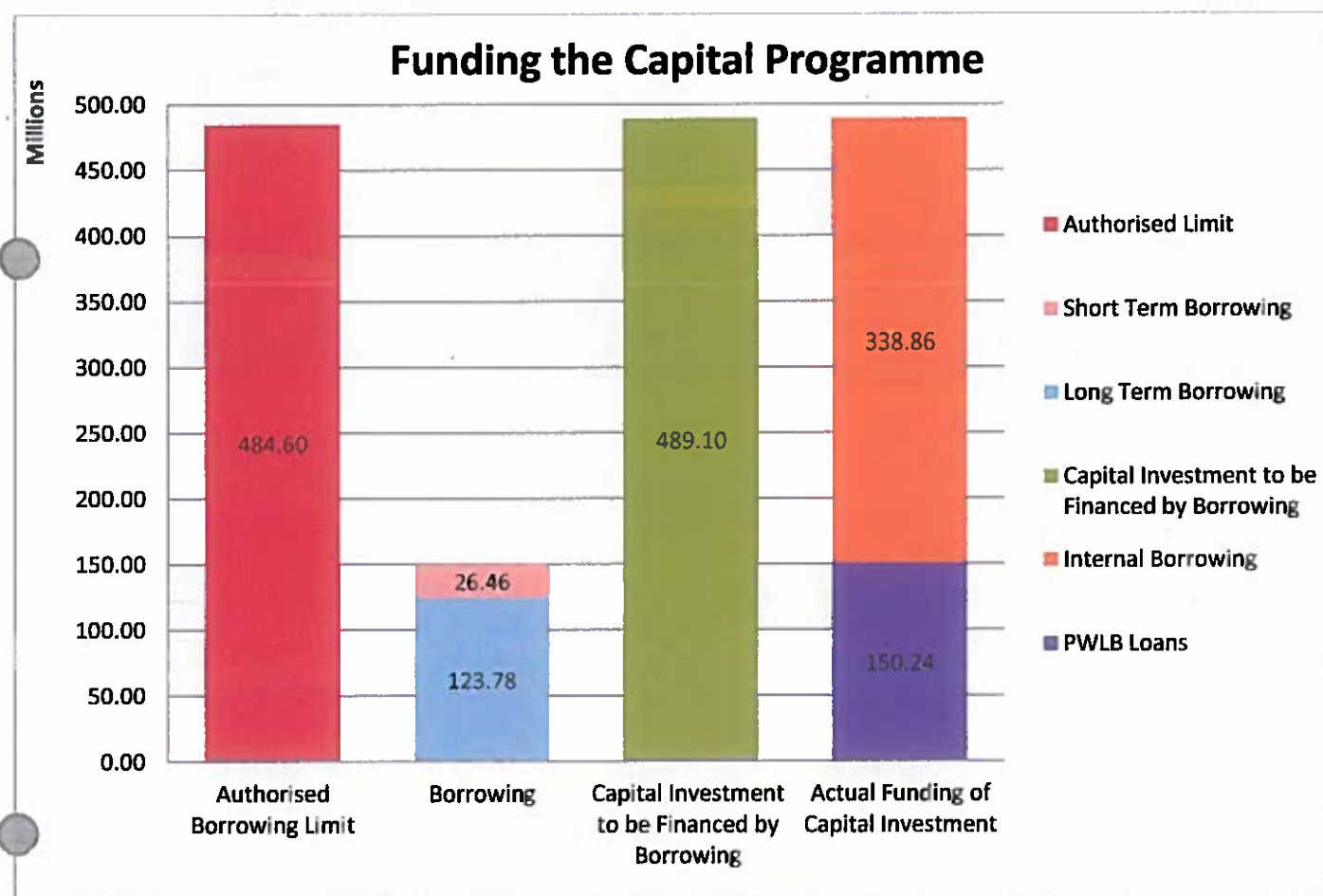
13 The table below shows the current Treasury management position.

Current Treasury Position	TMSS Forecast to 31 March 2018		Actual as at 30 September 2017		Revised Forecast to 31 March 2018	
	£m	Rate %*	£m	Rate %*	£m	Rate %*
External Borrowing						
Long-Term Borrowing: PWLB	359.60	4.33	150.24	4.23	143.01	4.33
Total External Borrowing (A)	359.60		150.24		143.01	
Other Long-Term Liabilities						
PFI Liability	74.06		76.00		74.06	
Finance Lease Liability	5.18		5.27		5.18	
Total Other Long-Term Liabilities (B)	79.24		81.27		79.24	
Total Gross Debt (A+B)	438.84		231.51		222.25	
Capital Financing Requirement	593.74		570.37		570.37	
Less Other Long-Term Liabilities	79.24		81.27		79.24	
Underlying Capital Borrowing Requirement (C)	514.50		489.10		491.13	
Under/(Over) Borrowing (C-A)	154.90		338.86		348.12	
Investments (D)	229.62	0.40	468.80	0.44	377.52	0.45
Total Net Borrowing (A-D)	129.98		-318.56		-234.51	

*Rate for borrowing is annualised yield; Rate for investments is cumulative average weighted yield

Borrowing Activity

- 14 No new external borrowing was undertaken during the six months ending 30 September 2017. PWLB loans of £9.23m were repaid, reducing total borrowing to £150.24m at 30 September 2017.
- 15 No rescheduling of debt was undertaken during the six months ending 30 September 2017.
- 16 The chart below compares the maximum MOPAC could borrow in 2017/18 with the 'capital investment to be financed by borrowing' at 31 March 2018 and the actual position of how this is being financed as at 30 September 2017.

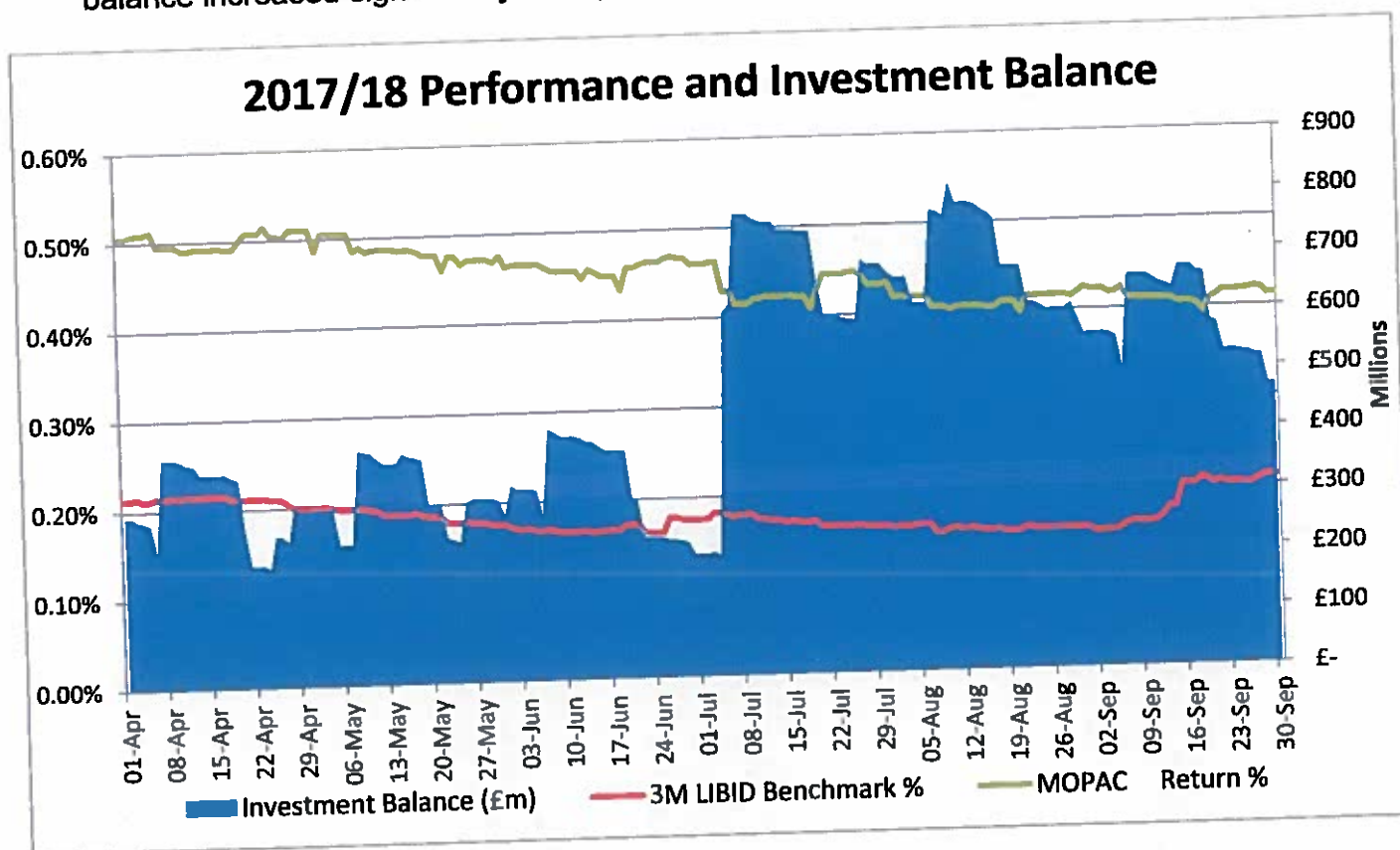


- 17 The chart shows that MOPAC's capital investment being financed by borrowing was £150.24m as at 30 September 2017. It also shows that MOPAC was using £338.86m of internal borrowing to finance capital investment.

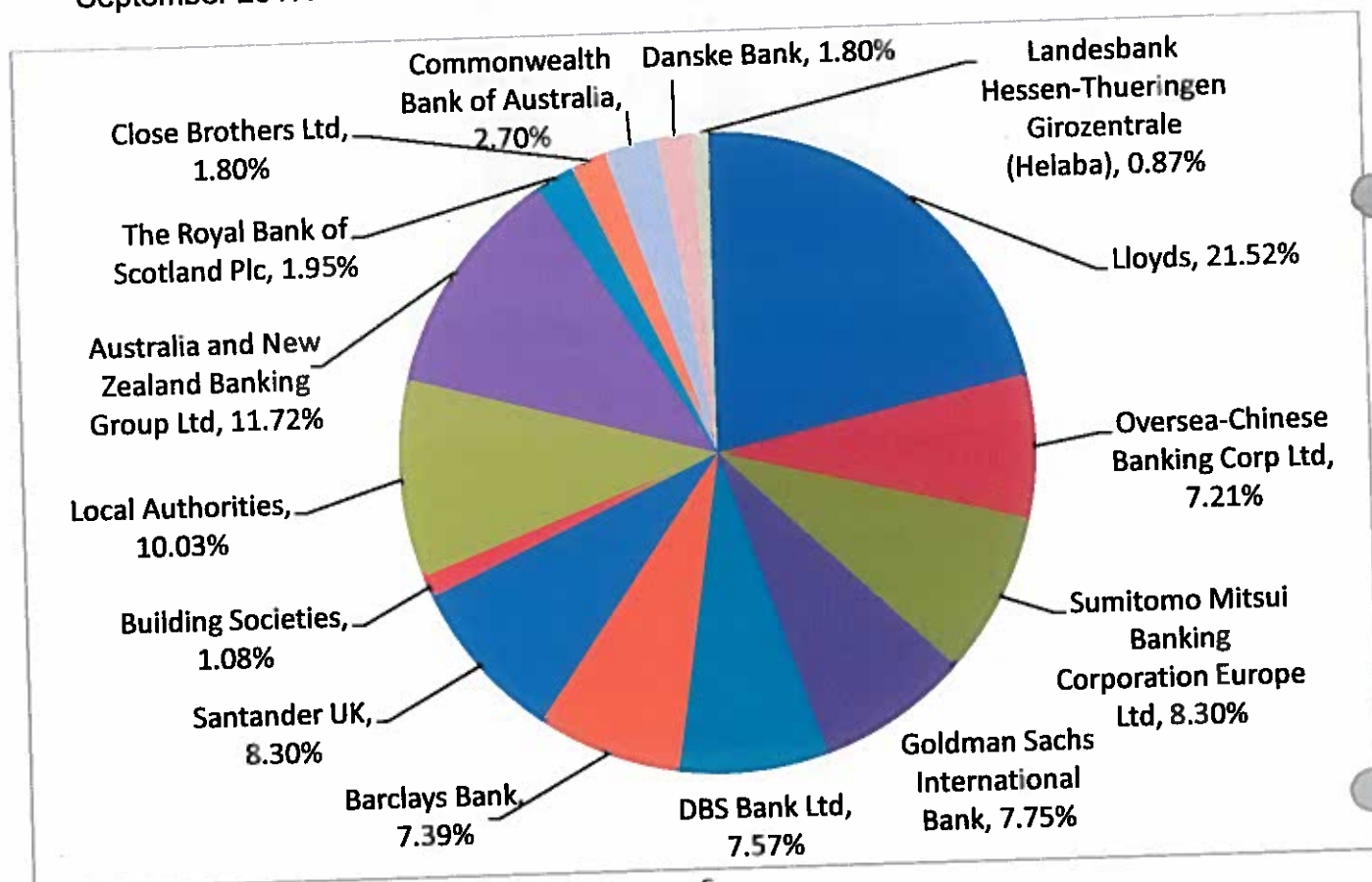
Investment Activity

- 18 Investment balances as at 30 September 2017 were £468.80m, this being an increase of £179.48m over the £289.32m opening balance on the 1 April 2017.
- 19 MOPAC has outperformed its investment benchmark by 0.26% during the six months ending the 30 September 2017. It has achieved a cumulative weighted average yield of 0.44% on daily balances against a cumulative weighted average 3 month LIBID of 0.18%.
- 20 Throughout the period, MOPAC maintained its liquidity target of a weighted average maturity (WAM) of not more than 91 days.

- 21 The following chart shows the outperformance described above, alongside MOPAC's total investment balances for the period. Fluctuations in balances reflect changes in cash flow requirements during the period, alongside the timing of grant receipts. The investment balance increased significantly in July due to the receipt of an annual pensions top-up grant.



- 22 The investment portfolio is well diversified as is demonstrated in the chart below, as at 30 September 2017.



Treasury Management Budget

Treasury Management Budget	2017-18 Original Estimate £m	2017-18 Actual As At 30.09.17 £m	2017-18 Revised Estimate £m	2017-18 Variance between Original Estimate and Revised Estimate £m
Interest payable : PWLB	6.84	3.23	6.40	0.44
Interest payable : Other Long Term Liabilities	13.38	6.21	12.42	0.96
Interest Receivable	-1.30	-1.04	-1.93	0.63
Total	18.92	8.41	16.89	2.03

- 23 The increase in forecast interest receivable of £0.63m against original estimate reflects a higher than expected investment balance alongside increasing deposit rates reflecting an anticipated interest rate rise.

CIPFA Prudential Code Indicators and Treasury Management Limits

- 24 The tables below show MOPAC's treasury position as at 30 September 2017, relative to the prudential indicator limits set in the 2017/18 Treasury Management Strategy.

- 25 All treasury activity for the period has been conducted within the limits set.

Capital Expenditure

Capital Expenditure	2017-18 Original Estimate £m	2017-18 Actual as at 30.09.17 £m	2017-18 Revised Estimate £m	2017-18 Variance between Original Estimate and Revised Estimate £m
Total Capital Expenditure	366.30	60.90	218.40	147.90

- 26 The reduction in forecast capital expenditure of £147.90m against original forecast has arisen due to slippage on the capital programme.

Capital Financing Requirement

Capital Financing Requirement (CFR)	2017-18 Original Estimate £m	2017-18 Actual as at 30.09.17 £m	2017-18 Revised Estimate £m	2017-18 Variance between Original Estimate and Revised Estimate £m
Total CFR	593.74	570.37	570.37	23.37

Authorised Limit for External Debt

Authorised Limit for External Debt	2017-18 Original Authorised Limit £m	2017-18 Actual External Debt as at 30.09.17 £m	Headroom £m	2017-18 Revised Authorised Limit £m
Borrowing	484.60	150.24	334.36	484.60
Other Long-Term liabilities	79.30	81.27	-1.97	79.30
Total	563.90	231.51	332.39	563.90

Operational Boundary for External Debt

Operational Boundary for External Debt	2017-18 Original Operational Boundary £m	2017-18 Actual External Debt as at 30.09.17 £m	Headroom £m	2017-18 Revised Operational Boundary £m
Borrowing	359.60	150.24	209.36	359.60
Other Long-Term liabilities	79.30	81.27	-1.97	79.30
Total	438.90	231.51	207.39	438.90

Gross Debt and the Capital Financing Requirement

2017-18 Actual Gross Debt as at 30.09.17 £m	Preceding Year CFR £m	2017-18 Estimated Additional CFR £m	2018-19 Estimated Additional CFR £m	2019-20 Estimated Additional CFR £m	Total CFR over 4 years £m	Amount Gross Debt < Total CFR over 4 years £m
231.51	611.93	0.00	68.86	88.36	769.15	537.64

Limits for Maturity Structure of Borrowing

Limits for Maturity Structure of Borrowing for 2017-18	Original Upper Limit	Original Lower Limit	As at 30.09.17
	%	%	%
Under 12 months	100.00	0.00	17.61%
12 months and within 24 months	100.00	0.00	13.33%
24 months and within 5 years	100.00	0.00	11.18%
5 years and within 10 years	100.00	0.00	17.31%
10 years and above	100.00	0.00	40.57%

New Investments Maturing after 364 days taken between 01/04/17 and 30/09/17

27 No new investment maturing after 364 days was undertaken between 1 April 2017 and the 30 September 2017.

New Long-Term Borrowing taken between 01/04/17 and 30/09/17

28 No new long-term borrowing was undertaken between 1 April 2017 and the 30 September 2017.