Treasury Management 2018/19 Outturn & Mid-year Report 2019/20

1. Introduction/Background

1.1. This report provides updates on both borrowing and investment activities of the treasury function under delegated authority for the financial year 2018/19 and mid-year to 30 September 2019.

1.2. Treasury management is defined as "the management of the Authority's borrowing, investments and cash flows; its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

1.3. Under the Authority's treasury management shared service arrangements, GLA treasury officers manage the Authority's day to day investments and borrowing activities.

2. London Treasury Limited (LTL)

2.1. In 2018/19, Greater London Authority Holdings Limited acquired LTL as a subsidiary company. The company is authorised and regulated by the Financial Conduct Authority to manage investments and provide investment advice. The company's purpose is to manage investments for the GLA group and enable the provision of treasury management services to other London Boroughs and/or relevant Local Authorities in the future.

2.2. A new pooled investment arrangement called the London Strategic Reserve (LSR) was created (for long term investments) during the year and the investments are being managed by LTL. £300m of GLA core balances has been allocated to the LSR. The existing Residential Mortgage Backed Securities (RMBS) investments and a new investment in Beechbrook are included as part of the LSR.

The objectives of the LSR are to:

- Preserve capital by ensuring that overall expected returns more than offset any reasonably foreseeable crystallised loss arising from individual investments elements of the portfolio over a rolling 5-year period;
- Achieve returns between 1-2% in excess of inflation (CPI) on a rolling 5-year basis in order to preserve spending power of long-term reserves;
- Harness the benefits of pooling to create less volatile cash balances, in turn allowing superior returns to be achieved through making less liquid investments;
- Use the specialist resources of LTL together with the GLA's panel of investment advisors to access investments requiring more complex consideration and due diligence than currently undertaken in order to access new opportunities and superior risk adjusted returns; and

- Engage in collaborative lending within London to reduce net financing costs across the capital.

3. Treasury Management Strategy Statement (TMSS) 2018/19 and 2019/20

3.1. The Executive Director of Resources confirms that, throughout the reporting period, all treasury activities have been conducted within the parameters of the Treasury Management Strategy Statement.

3.2. The TMSS was amended during the year to establish the London Strategic Reserve (LSR). The amendment enabled the GLA to create a seed portfolio for the LSR.

4. Treasury Management Outturn Position for 2018/19 and mid-year 2019/20

Summary Portfolio Position

Current Treasury Management Position	**Actual as at 31.03.2018**		**Actual as at 31.03.2019**		**Actual as at 30.09.2019**	
	£m	Rate %	£m	Rate %	£m	Rate %
External Borrowing						
Long Term Borrowing	3,771.58	3.42	4,231.61	3.28	4,699.60	3.14
Variable Rate Borrowing	26.46	0.65	23.51	0.96	26.71	0.90
Total External Borrowing (A)	**3,798.04**		**4,255.12**		**4,726.31**	
Other Long-Term Liabilities						
PFI Liability	-		-		-	
Finance Lease Liability	-		-		-	
Total Other Long-Term Liabilities (B)	-		-		-	
Total Gross Debt (A+B)	**3,798.04**		**4,255.12**		**4,726.31**	
Capital Financing Requirement	3,800.44		4,242.69		5,293.22	
Less Other Long-Term Liabilities	-		-		-	
Underlying Capital Borrowing Requirement (C)	**3,800.44**		**4,242.69**		**5,293.22**	
Under/(Over) Borrowing (C-A)	2.40		12.43		566.91	
Investments: Short/Long Term (D)	2,183.38	0.58	2,772.25	0.90	3,488.27	0.93
Total Net Borrowing (A-D)	**1,614.66**		**1,482.86**		**1,238.05**	

5. Borrowing Activity:

5.1. The Authority is required to borrow to fund its capital programme. The amount of new borrowing needed each year is determined by new capital schemes approved and included in the capital programme. Temporary borrowing is required to manage operational cashflow requirements. The following table shows the movement in borrowing during the reporting period and the split of borrowing between the GLA, Crossrail and the Northern Line Extension.

	Long Term (LT) Borrowing			Total LT Borrowing	Variable Rate/ST Borrowing LWARB/OPDC	Total
	GLA £m	Crossrail £m	NLE £m	£m	£m	£m
Balance at 31.03.18	**255.00**	**3,067.50**	**449.08**	**3,771.58**	**26.46**	**3,798.04**
Add New Loans in 2018/19	-	365.00	245.02	610.02	42.40	652.42
Less Loans Repaid in 2018/19	25.00	(125.00)	-	(150.00)	(45.35)	(195.35)
Balance at 31.03.19	**230.00**	**3,307.50**	**694.10**	**4,231.60**	**23.51**	**4,255.12**
Add New Loans in 2019/20	-	363.00	200.00	563.00	5.09	568.10
Less Loans Repaid in 2019/20	-	(95.00)	-	(95.00)	(1.90)	(96.90)
Balance at 30.09.19	**230.00**	**3,575.50**	**894.10**	**4,699.60**	**26.71**	**4,726.31**

6. Long Term (LT) Borrowing:

6.1. A total of £610.02m long term borrowing was taken during 2018/19. This was made up of additional borrowing for Crossrail of £365m and the Northern Line Extension (NLE) of £245.02m. In 2019/20, £563m was taken as at 30 September, this was made up of £363m for Crossrail and £200 NLE borrowing.

6.2. **Borrowing (Crossrail)**- The GLA entered into a loan agreement for a total of £1.3bn with the Department for Transport (DfT) as part of the funding for Crossrail's cost overruns identified in December 2018. A total of £365m was drawn from the amount in 2018/19 and a further £363m was taken in 2019/20 as at 30 September 2019.

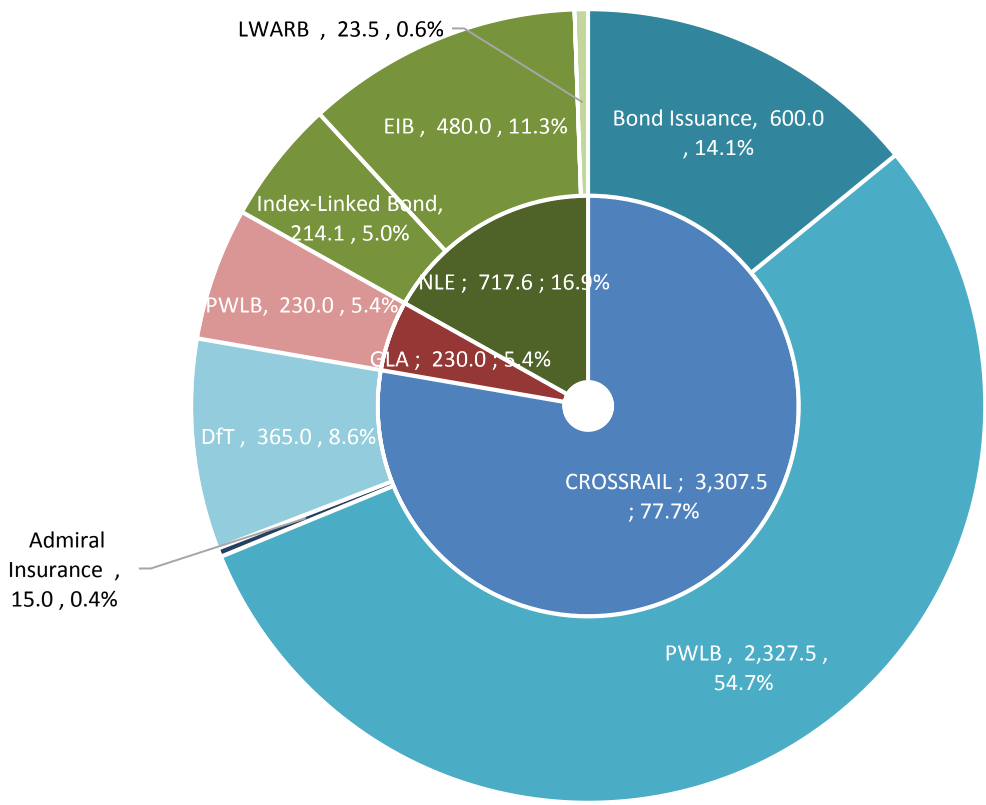
6.3. **Borrowing (NLE)**- The £245.02 NLE new borrowing in 2018/19 is made up of a £240m loan from the European Investment Bank (EIB) and an uplift on the existing index-linked Community Finance Bonds of £5.02m. The bond is linked to the Consumer Price Index (CPI) and the uplift was as a result of an increase in the CPI figure from 104.1 in September 2017 to 106.6 in September 2018. A further £200m was borrowed from the Public Works Loan Board (PWLB) in May 2019 with a weighted average maturity of some 12.6 years and a weighted average interest rate of 2.03%.

6.4. **Repayments**- A total of £150m was repaid during 2018/19, made up of £25m of GLA PLWB loans and £125m of Crossrail PWLB and market loans. As at the 30 September 2019 a total of £95m of Crossrail PWLB and market loans have been repaid.

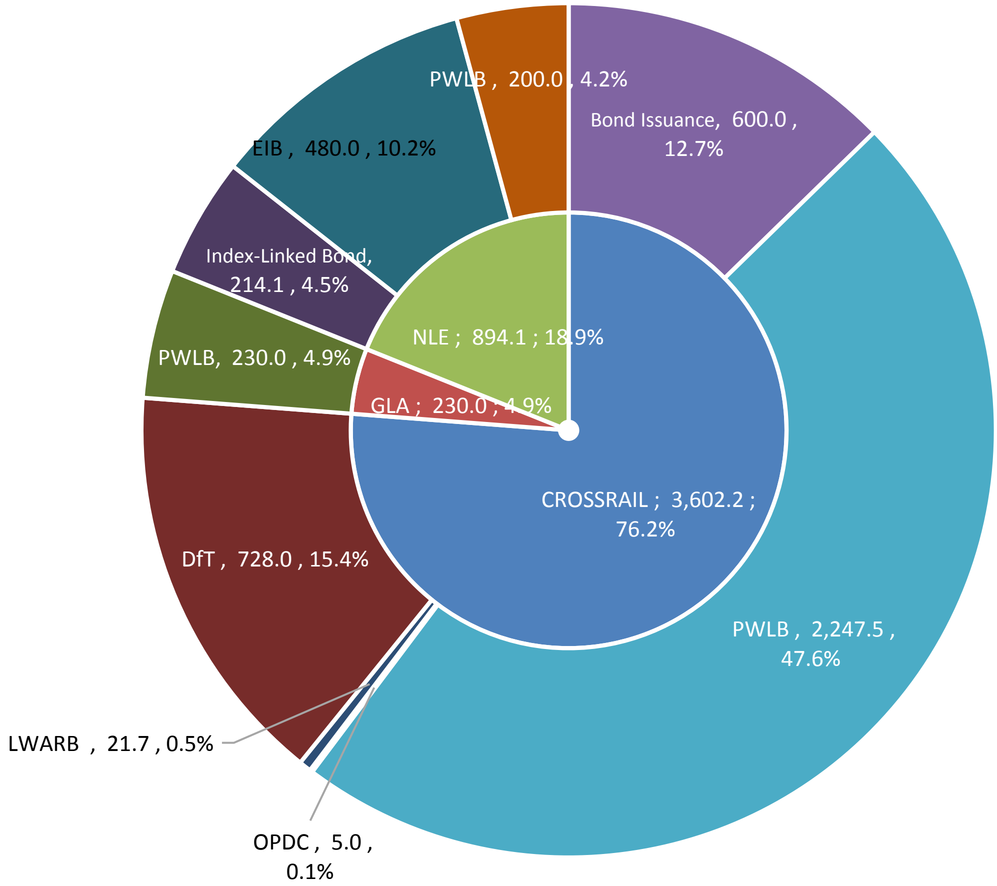
6.5. The closing balance of long-term loans at the 31 March 2019 was £4,231.60m and £4,699.50m as at 30 September 2019.

7. Short Term/Variable rate Borrowing

7.1. Short term borrowings were taken and repaid to manage cash flow during the reporting periods. LWARB variable rate borrowing had a balance of £23.51m as at 31 March 2019 and £21.67m as at 30 September 2019. In April 2019, the GLA took £5.04m of OPDC s106 cash as a variable rate borrowing after a mutual agreement was signed by both parties.The following charts show the structure of GLA's loan portfolio as at 31 March 2019 and 30 September 2019.



GLA Loan Portfolio (£m) as at 30.09.2019



8. Investment Activities

8.1. During the reporting period, the Authority invested the majority of its surplus cash on a temporary basis (i.e. up to 365 days) through the GLA Group Investment Syndicate (GIS). The remaining balance was invested for longer than 365 days through LSR in Residential Mortgage Backed Security (RMBS) and a discrete investment called Beechbrook which is described below. RMBS investment has a weighted Average maturity (WAM) of three years.

8.2. **Beechbrook** - The Authority entered into a Limited Partnership with Beechbrook UK SME Credit II LP (Beechbrook) to invest a total sum of £20m. A proportion of the £20m commitment will be drawn down as and when investment opportunity becomes available. The balance of investment in Beechbrook was £2.02m as at 31 March 2019. The fund investment forms part of LSR. The balance as at 30 September 2019 was £5.03m.

8.3. The table below shows a split between investment balances for the periods.

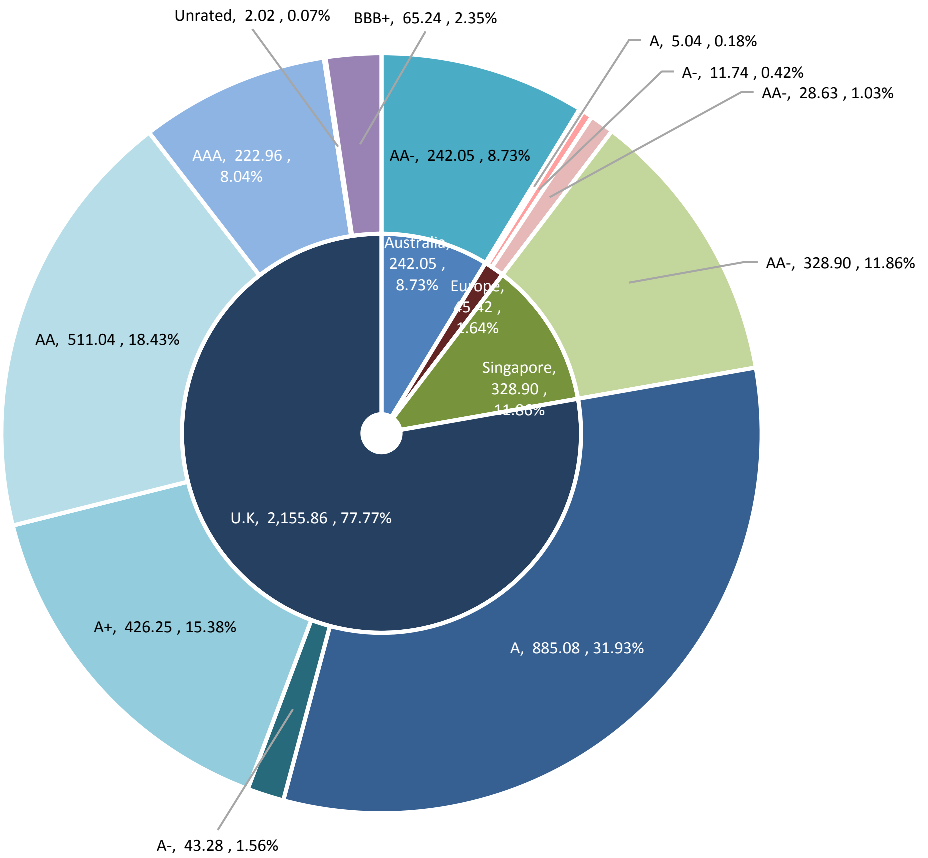
Investments	Long Term - (RMBS) £m	Short Term £m	Total £m
Balance at 01.04.18	229.56	1,953.82	2,183.38
Balance at 31.03.19	223.95	2,548.31	2,772.25
Balance at 30.09.19	228.53	3,259.73	3,488.27

8.4. Investment balances during 2018/19 increased from £2,183.38m to £2,772.25m as at 31 March 2019, representing an increase of £588.87m (27%) during the reporting periods. The balance at the 30 September 2019 has increased by a further of £711.43 (25.83%) to £3,488.27m. The increase was due to the profile of Affordable Housing Grants provided by the Government.

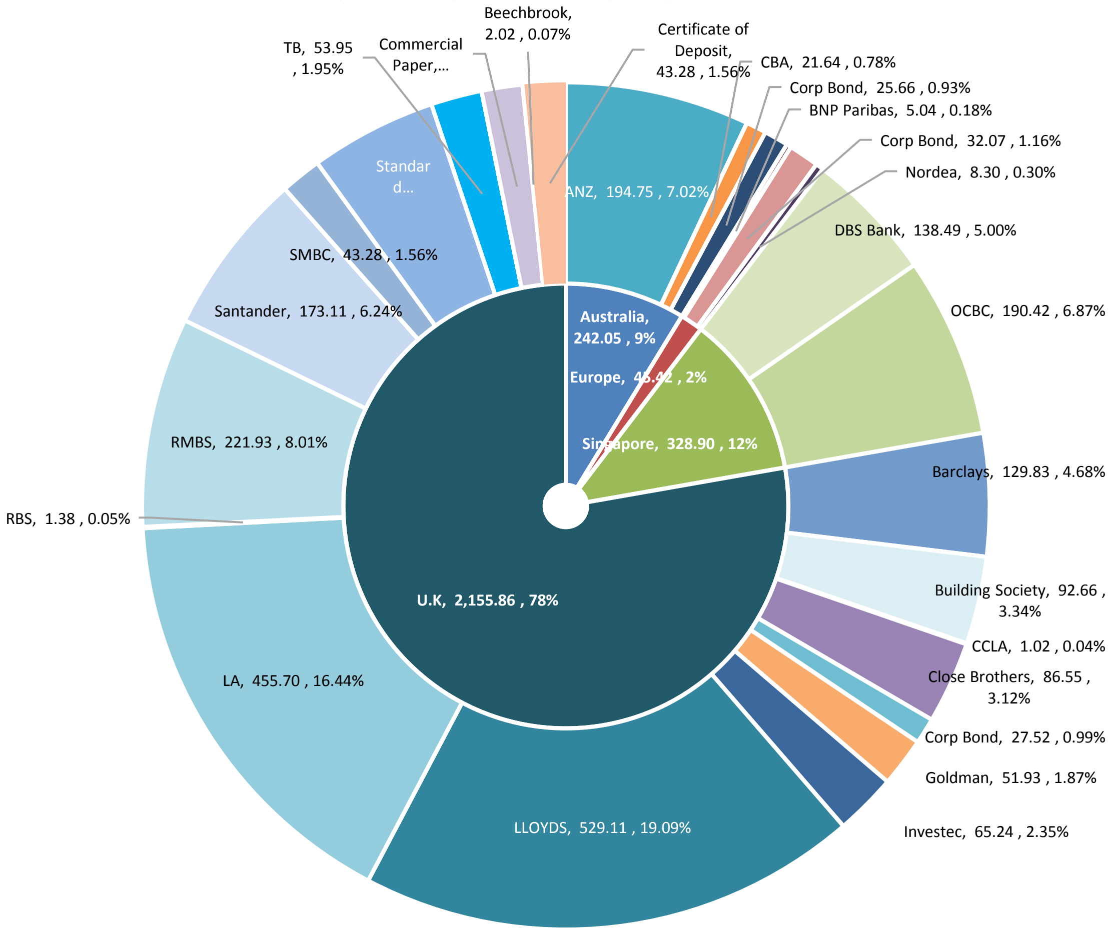
8.5. All investments were made in line with the GLA Investment Strategy, which includes the requirement to maintain a weighted average maturity (WAM) of three months for short term investment and three years for long-term (RMBS) investment.

8.6. The following charts provide a breakdown of investments by Country versus Credit rating and Counterparty as at 31 March 2019 and 30 September 2019, showing a well-diversified and balanced investment portfolio.

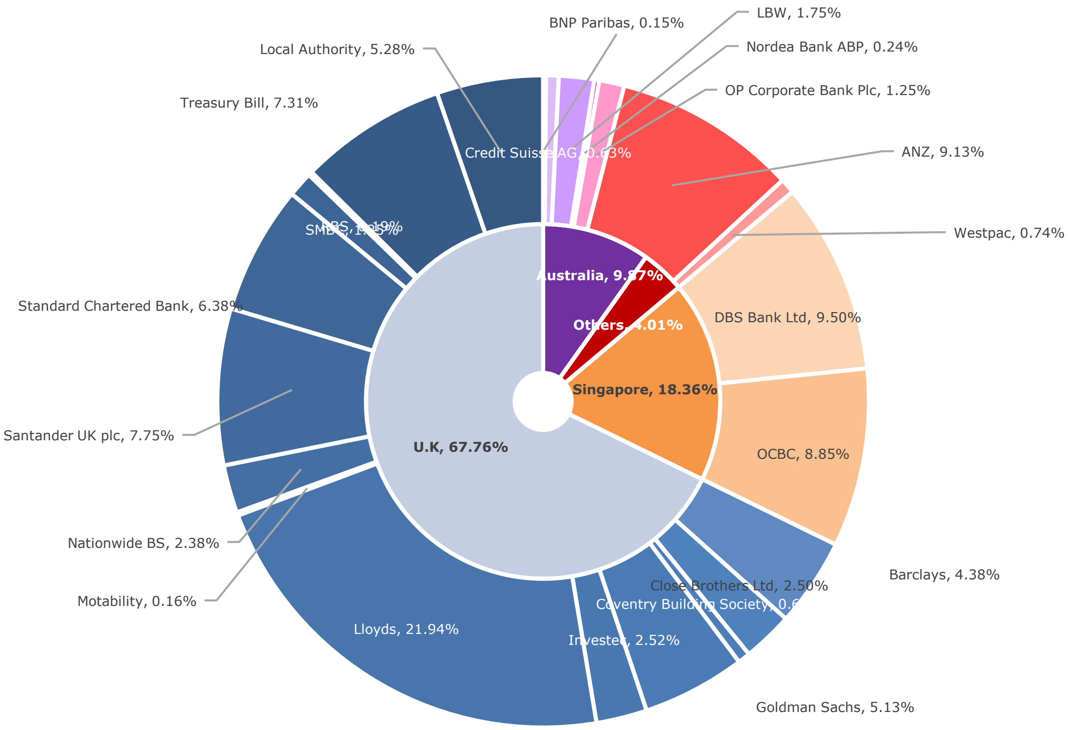
Investment by Country & Credit Rating 31 March 2019 (£m)



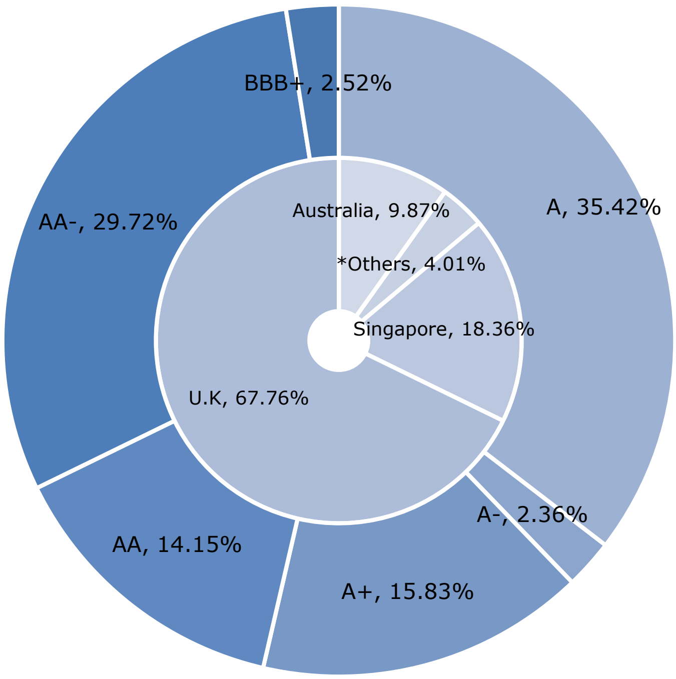
Investment By Country & Counterparty 31 March 2019 (£m)



Investment by Country and Counterparty 30 September 2019 (£m)



Investment by Country and Credit Rating 30 September 2019



9. Investment Performance

i) Short Term Investment

9.1. Returns earned on short-term investments during the 2018/19 financial year equated to £16.50m against a budget of £11m, an outperformance of £4.50m (41%). The Authority's weighted average investment return was 0.85% in 2018/19 against weighted average 3-month LIBID rate of 0.68%, the GLA outperforming its benchmark by 0.17%. As at 30 September 2019 returns on short-term balances were £13.31m. Weighted average investment return was 0.97% against LIBID benchmark of 0.66%, an outperformance of 0.31%. The liquidity target of a weighted average maturity (WAM) of not more than three months was maintained throughout the reporting periods.

9.2. The GIS benchmarks against the average 3-month LIBID. This is a comparable performance indicator for the GIS investment return. The LIBID is the London Interbank Bid Rate; it is the interest rate at which major banks in London are willing to borrow (bid for) funds from each other.

ii) Long Term Investments

9.3. **RMBS** -The RMBS investment achieved a cumulative performance of 1.46%, resulting in investment return of £3.29m against a budget of £2m in 2018/19. The investment has a targeted WAM of three years and it maintained a WAM of lower than the three years throughout the reporting period. The performance of 1.45% was achieved in 2019/20 mid-year, with the return being £1.67m.

9.4. **Beechbrook** – The investment in Beechbrook has a carrying value of £2.015m and a fair value of £2.031m at the end of the year. Return on the investment will be paid annually when the fund is in position to disburse returns to investors, it is anticipated this will commence two or three years from the date of investment. A further £3.01m was invested in Beechbrook resulting in a carrying value of £5.03m as at 30 September 2019. Fair value will be calculated at the year end.

9.5. The treasury function achieved a total return of £19.79m on investments, outperforming the investment income budget of £13m by some £6.79m in 2018/19. In 2019/20 mid-year, the return was £14.98m against a budget of £6.85m.

9.6. RMBS contributed an additional £1.38m to the £19.79m return in 2018/19 and £0.56m to the £14.98m return in the half year of 2019/20. Therefore, returns would have been £18.41m and £14.42m in 2018/19 and 2019/20 respectively without these investments. RMBS has contributed £3.62m of incremental value since inception while only constituting an average of 10% of the total portfolio.

Treasury Management Financing costs

	Actual as at 31.03.19 £m	**Actual as at 30.09.19 £m**
Interest Payable: PWLB, Bonds and Market Loans	132.07	72.24
Interest Payable: Other LT Liabilities	-	-
Total Interest Receivable	(19.79)	(14.98)
Minimum Revenue Provision (MRP) & Vol Revenue Provision	202.10	96.90
Total	314.38	154.16

The Authority paid a total of £132.07m in financing cost in 2018/19 and a total of £72.24m in the half-year to September 2019. Actual MRP for 2018/19 amounted to £202.10m and the £96.90m reported for half year of 2019/20 represents total loan repayments to the 30 September.

10. CIPFA Prudential Code Indicators and Treasury Management Limits

10.1. The Prudential Code has been developed to support Local Authorities in taking decisions on capital investment. Key objectives of the Code are to ensure, within a clear framework, that Local Authorities' capital investment plans are affordable, prudent and sustainable; that treasury management decisions are taken in accordance with good professional practice; and that local strategic planning, asset management planning and proper option appraisal are supported. These Prudential Indicators are set out below.

11. Capital Expenditure

11.1. Capital expenditure results from the approved capital spending plan and proposed borrowing limits.

	2018/19 Budget £m	**2018/19 Actual £m**	**2018/19 Variance £m**
Capital Expenditure	1,124.70	1,636.90	(512.20)
Capital Financing Requirement	3,890.44	4,242.69	(352.25)

	2019/20 Budget £m	**2019/20 30.09.2019 Actual £m**	**2019/20 Variance £m**
Capital Expenditure	2,419.04	692.10	(1,726.94)
Capital Financing Requirement	5,293.22	4,699.60	(593.62)

iii) Capital Financing Requirement

11.2. The capital financing requirement (CFR) is an indicator of the underlying need to borrow for capital purposes. It is the capital expenditure which has been incurred but not yet paid for. Any new capital expenditure in the year, which is not immediately paid for, will increase the CFR.

12. External Debt Prudential Indicators

iv) Authorised Limit for External Debt

Authorised Limit for External Debt	2018/19 Authorised Limit £m	2018/19 External Debt as at 31.03.2019 £m	Headroom £m
Borrowing	4,800.00	4,255.12	544.88
Total	4,800.00	4,255.12	544.88

Authorised Limit for External Debt	2019/20 Authorised Limit £m	2019/20 External Debt as at 30.09.2019 £m	Headroom £m
Borrowing	6,100.00	4,726.31	1,373.69
Total	6,100.00	4,726.31	1.373.69

v) Operational Boundary for External Debt

	2018/19 Operational Boundary £m	2018/19 External Debt as at 31.03.2019 £m	Headroom £m
Borrowing	4,300.00	4,255.12	44.88
Total	4,300.00	4,255.12	44.88

	2019/20 Operational Boundary £m	2019/20 External Debt as at 30.09.2019 £m	Headroom £m
Borrowing	5,700.00	4,726.31	973.69
Total	5.700.00	4,726.31	973.69

vi) Limits for Maturity Structure of Borrowing

	Upper Limit %	Lower Limit %	31.03.2019 %
Under 12 months	10	0	3.51
12 months and within 2 years	10	0	2.16
2 years and within 5 years	10	0	20.20
5 years and within 10 years	45	15	29.02
10 years and above	100	50	45.10

	Upper Limit %	Lower Limit %	30.09.2019 %
Under 12 months	10	0	7.76
12 months and within 2 years	10	0	6.19
2 years and within 5 years	20	0	15.55
5 years and within 10 years	45	15	31.17
10 years and above	100	50	39.34

12.1. These indicators show the ranges for the expected maturity profile of the borrowing portfolio, based on the GLA's existing borrowing, expected new borrowing and availability of resources for repayment.

12.2. For the largest borrowing element, related to Crossrail, the GLA's assumptions changed significantly in 2018/19 as a result of a material overspend being identified and the decision to use more of the Mayoral Community Infrastructure Levy (MCIL) alongside the BRS to repay this debt. A special borrowing facility and repayment profile was agreed with DfT in Dec 2018 to cover the overspend.

12.3. As a result of the new circumstances the loan balance within two to five years exceeded our estimated range while the percentage of loans maturing in more than ten years fell below the estimated range in 2018/19.

12.4. The new assumptions were reflected in the ranges set out in the 2019/20 strategy. All borrowing maturities were within the estimated ranges as at 30 September 2019.

13. Event after reporting date

13.1. <u>PWLB Interest Rate Increase</u>

HMT increased their margin on PWLB borrowing by one percentage point in October 2019, taking the cost of general borrowing by the GLA from the PWLB to 1.8% above Gilts. This is now much more expensive than the margins achieved by the GLA in recent borrowing from the capital markets, therefore the GLA expects to rely more on alternatives to the PWLB in future.