ANNEX I

TREASURY MANAGEMENT ANNUAL REPORT 2019/20

1. Purpose

1.1. Local authorities are under legal obligation by the Local Government Act 2003 to have regard to the treasury risk management framework of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services: Code of Practice 2017 Edition (the Code). The Council is also required to have regard to Ministry of Housing, Communities and Local Government (MHCLG) guidance in relation to Investments and Minimum Revenue Provision (MRP).

1.2. The Code requires, as a minimum, the Council to report:

a) an annual treasury strategy in advance of the year; presented to Council on 20/02/2019;

b) a mid-year (minimum) treasury update report; delegated decision by Cabinet on 23/12/2019;

c) an annual report following the end of the year describing the activity undertaken compared to the strategy; this report.

1.3. During 2019/20 and in line with best practice principles, the Council also presented quarterly update reports to Cabinet on 03/09/2019 for Q1 & 10/03/2020 for Q3.

1.4. The CIPFA Prudential Code for Capital Finance in Local Authorities (2017 Edition) includes a requirement for local authorities to produce a Capital Strategy, a summary document to be approved by Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy was also approved by Council on 20/02/2019.

2. External Context

Economic background:

2.1. The UK's exit from the European Union and future trading arrangements had remained one of major influences on the UK economy and sentiment during 2019/20. The 29th March 2019 Brexit deadline was extended to 12th April, then to 31st October and finally to 31st January 2020. The political backdrop played a major role in financial markets over the period as the UK's tenuous progress negotiating its exit from the European Union together with its future trading arrangements drove volatility, particularly in foreign exchange markets. The outcome of December's General Election removed a lot of the uncertainty and looked set to provide a 'bounce' to financial market confidence and activity.

2.2. The headline rate of UK Consumer Price Inflation UK Consumer Price Inflation fell to 1.7% y/y in February, below the Bank of England's target of 2%. Labour market data remained positive. The ILO unemployment rate was 3.9% in the three months to January 2020 while the employment rate hit a record high of 76.5%. The average annual growth rate for pay excluding bonuses was 3.1% in January 2020 and the same when bonuses were included, providing some evidence that a shortage of labour had been supporting wages.

2.3. GDP growth in Q4 2019 was reported as flat by the Office for National Statistics (ONS) and service sector growth slowed and production and construction activity contracted on the back of what at the time were concerns over the impact of global trade tensions on economic activity. The annual rate of GDP growth remained below-trend at 1.1%.

2.4. Then coronavirus swiftly changed everything. COVID-19, which had first appeared in China in December 2019, started spreading across the globe causing plummeting sentiment and falls in financial markets (not seen since the Global Financial Crisis 2008) as part of a 'flight to quality' into sovereign debt and other perceived 'safe' assets.

2.5. In response to the spread of the virus and sharp increase in those infected, Governments including the UK enforced lockdowns, and together with central banks around the world cut interest rates and introduced massive stimulus packages in an attempt to reduce some of the negative economic impact to domestic and global growth and help businesses and households impacted by a series of ever-tightening social restrictions.

2.6. The Bank of England (BoE), which had held policy rates steady at 0.75% through most of 2019/20, moved in March to cut rates to 0.25% from 0.75% and then swiftly thereafter brought them down further to the record low of 0.10%.

2.7. The US economy grew at an annualised rate of 2.1% in Q4 2019. After escalating trade wars and a protracted standoff, the signing of Phase 1 of the trade agreement between the US and China in January was initially positive for both economies, but COVID-19 severely impacted sentiment and production in both countries. Against a slowing economic outlook, the US Federal Reserve began cutting rates in August. Following a series of five cuts, the largest of which were in March 2020, the Fed Funds rate fell from of 2.5% to range of 0% - 0.25%. The US government also unleashed a raft of COVID-19 related measures and support for its economy including a $2 trillion fiscal stimulus package.

2.8. With interest rates already on (or below) the floor, the European Central Bank held its base rate at 0% and deposit rate at -0.5%.

Financial markets:

2.9. After starting positively in 2020, there was a sharp sell-off as the impact from the coronavirus worsened. The FTSE 100 fell over 30% at its worst point with stock markets in other countries seeing similar huge falls. In March sterling touched its lowest level against the dollar since 1985. The measures implemented by central banks and governments helped restore some confidence and financial markets rebounded in mid-April 2020 but remain extremely volatile.

2.10. The 'flight to quality' caused gilts yields to fall substantially, with the 5-year benchmark falling from 0.75% in April 2019 to 0.26% in March 2020. In the same period, the 10-year benchmark yield fell from 1% to 0.4%, the 20-year benchmark yield from 1.47% to 0.76%. 1-month, 3-month and 12-month inter-bank lending 'bid' rates averaged 0.61%, 0.72% and 0.88% respectively over the period.

2.11. Since the start of the calendar year 2020, the yield on 2-year US treasuries had fallen from 1.57% to 0.20% and from 1.88% to 0.61% for 10-year treasuries. German bund yields remain negative.

Credit background:

2.12. In Q4 2019, rating agency Fitch affirmed the UK's AA sovereign rating, removed it from Rating Watch Negative (RWN) and assigned a negative outlook. Fitch then affirmed UK banks' long-term ratings, removed the RWN and assigned a stable outlook. Standard & Poor's also affirmed the UK sovereign AA rating and revised the outlook to stable from negative. The Bank of England announced its latest stress tests results for the main seven UK banking groups. All seven passed on both a common equity Tier 1 (CET1) ratio and a leverage ratio basis. Under the test scenario, a banks' aggregate level of CET1 capital would remain twice their level held before the 2008 financial crisis.

2.13. A Credit Default Swap (CDS) is a form of market insurance policy taken to compensate the holder in the event of a debt default or other credit event. As an actively traded market, sharp movements may indicate early signs of financial distress. CDS markets remained largely flat in January and February then rose sharply in March, as the potential impact of the coronavirus on bank balance sheets gave cause for concern. Markets declined in late March and through to mid-April but remain above their initial 2020 levels.

2.14. In response to the uncertain credit environment, in February 2020 officers took the decision to avoid new term deposits with banking institutions. The select UK and non-UK banks & building societies that the Council considers suitable investment counterparties remain in strong and well-capitalised positions, so pre-existing deposits are being allowed to run until maturity.

2.15. In March 2020, using the Council's treasury advisors method of applying a financial strength rating based on published financial data, officers agreed loans ranging from 90 days to 2 years totalling £35m with a select number of other local authorities. The financial strength ratings are categorised as 'gold', 'silver' and 'bronze' which recognises that all local authorities are good credit, albeit to varying degrees of perceived strength. Officers set a minimum rating floor of 'silver'. These loans have allowed the Council to diversify a proportion of its investment portfolio with strong counterparties at above market rates of return.

2.16. The remainder of surplus cash and banking institution maturities are instead being invested in either;

a) short-term liquid money market fund and bank call account instruments, with increased daily monitoring measures in place; or

b) short-term deposits direct with UK Government's Debt Management Office.

2.17. In mid-March the Council's treasury advisors reduced recommended duration advice on all global banks and building societies from up to 12 months in some cases to a maximum of up to 35 days across the board. The Council is guided by this professional advice but not bound to it and investment decisions remain the responsibility of the Council at all times. In this case officers agree that this recommended risk-aversion action is necessary but does consequently severely restrict the investment options available to the Council. It is likely therefore in the short-term that as existing market investments mature, the Council's holdings with the UK Government's Debt Management Office (no upper counterparty limit) will increase.

2.18. The Council also utilises AAA rated Money Market Funds for short-term liquid cash investments. These pooled funds represent well-diversified, same-day access options with assets under management usually in the tens of billion pounds at any given time from many business sectors, including local authorities. Each fund with assets of more than one billion pounds under management is considered by the Council as comparatively secure as its peers, yet the Council limits investments to up to £15m per fund to spread counterparty risk. Nonetheless during March officers stepped up monitoring of these funds performance given the widespread financial market volatility and uncertainty from the impact of COVID-19. The difference in return between individual funds is at present marginally low, so in this heightened state of alert, added emphasis is instead being placed on the stability of each fund's underlying total assets on a running daily and weekly basis as the primary influence to investment or withdrawal considerations. This enhanced monitoring process led to officers recalling the full balance of investments from one particular fund due to asset volatility as a precautionary measure, ahead of a subsequent recommendation to this effect from the Council's treasury advisors.

2.19. Fitch downgraded the UK sovereign rating to AA- in March which was followed by a number of actions on UK and Non-UK banks. This included revising to negative the outlook on all banks on the Council's filtered list of possible counterparties, with the exception of Barclays Bank, Rabobank, Handelsbanken and Nordea Bank which were placed on Rating Watch Negative, as well as cutting Close Brothers long-term rating to A-. Having revised their outlooks to negative, Fitch upgraded the long-term ratings on Canadian and German banks but downgraded the long-term ratings for Australian banks. HSBC Bank and HSBC UK Bank, however, had their long-term ratings increased by Fitch to AA-.

3. <u>Annual Investment Strategy</u>

3.1. The Treasury Management Strategy Statement (TMSS) for 2019/20, which includes the Annual Investment Strategy, was approved by the Council on 20th February 2019. It sets out the Council's fundamental investment priorities as being (in order):

1. **S**ecurity of Capital;
2. **L**iquidity; and
3. **Y**ield

3.2. Interest rates expectations within the 2019/20 strategy anticipated low but rising Bank Rate, with gradual rises in medium and longer term fixed borrowing rates. Continued market risks promoted a cautious approach to investments, whereby options would continue to be dominated by a low counterparty risk appetite, resulting in relatively low returns (when compared to borrowing rates) in achieving low risk. Notwithstanding the Councils strategic approach to avoid new borrowing, short-term borrowing rates were expected to be the cheapest form of borrowing should the situation have changed and funds needed to be raised.

4. Borrowing

4.1. The Council's primary objective when borrowing is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should long-term plans change is a secondary objective.

4.2. On 9th October 2019 and without prior warning, the Public Works Loans Board (PWLB) raised the margin cost of the concessionary 'certainty' rate borrowing by 1% as HM Treasury was concerned about the overall level of local authority debt. This decision was met with widespread condemnation given the negative unintended consequence on tightly costed schemes, such as housing and regeneration. PWLB borrowing remains available, but the margin of 1.8% above gilt yields appears relatively expensive compared to market alternatives.

4.3. The Government's March 2020 Budget statement included significant changes to PWLB policy and launched a wide-ranging consultation on the PWLB's future direction. Announcements included a reduction in the margin on new HRA loans to 0.80% above equivalent gilt yields (the value of this discount is 1% below the rate at which the Council could borrow from the PWLB) and £1.15bn of additional 'infrastructure' rate funding available at gilt yields plus 0.60% to support pre-approved specific local authority infrastructure projects following an application process.

4.4. The consultation on the future of the PWLB allows key stakeholders to contribute to developing a system whereby PWLB loans can be made available at improved margins to support projects that meet certain qualifying criteria. Proposals include allowing authorities that are not involved in 'debt for yield' activity to borrow at lower rates, as well as measures to stop local authorities using PWLB loans to buy commercial assets primarily for yield, without impeding their ability to pursue their core policy objectives. The consultation also broaches the possibility of slowing, or stopping, individual authorities from borrowing large sums in specific circumstances.

4.5. The Director of Finance and Resources will respond to the consultation on behalf of the Council. The consultation closes on 4th June 2020 with implementation of the new lending terms expected in the latter part of this calendar year or financial year beginning 2021/22. Further updates will be reported through Treasury Management Update reports as they develop.

4.6. Tables 1 below sets out the profile of the Council's borrowing portfolio by source of loan:

Table 1: Borrowing profile at 31st March 2020 by loan source

Tenor Bucket	Market Loans		PWLB Loans		Total	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Liquid	£0.00	0.0%	£0.00	0.0%	£0.00	0.0%
< 1 Year	£5,000,000.00	33.3%	£7,027,124.81	1.6%	£12,027,124.81	2.6%
1 - 2 Years	£0.00	0.0%	£9,732,747.02	2.2%	£9,732,747.02	2.1%
2 - 5 Years	£0.00	0.0%	£39,648,657.81	8.8%	£39,648,657.81	8.5%
5 - 10 Years	£0.00	0.0%	£64,697,089.19	14.4%	£64,697,089.19	13.9%
10 - 20 Years	£0.00	0.0%	£141,933,076.58	31.4%	£141,933,076.58	30.5%
20 - 30 Years	£0.00	0.0%	£27,000,000.00	6.0%	£27,000,000.00	5.8%
30 - 40 Years	£0.00	0.0%	£109,000,000.00	24.2%	£109,000,000.00	23.4%
40 - 50 Years	£10,000,000.00	66.7%	£51,360,000.00	11.4%	£61,360,000.00	13.2%
> 50 Years	£0.00	0.0%	£0.00	0.0%	£0.00	0.0%
Total	**£15,000,000.00**	**100.0%**	**£450,398,695.41**	**100.0%**	**£465,398,695.41**	**100.0%**

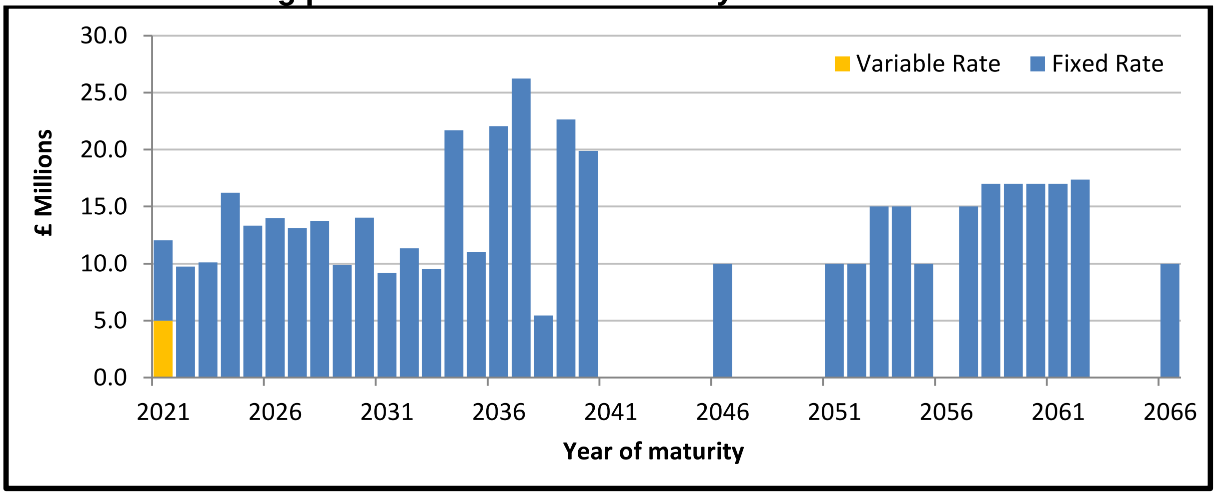
4.7. Tables 2 below sets out the profile of the Council's borrowing portfolio by interest rate structure/exposure:

Table 2: Borrowing profile at 31st March 2020 by interest rate structure

Tenor Bucket	Fixed Rate Loans	% of Total	Variable Rate Loans	% of Total	Total	% of Total
Liquid	£0.00	0.0%	£0.00	0.0%	£0.00	0.0%
< 1 Year	£7,027,124.81	1.5%	£5,000,000.00	100.0%	£12,027,124.81	2.6%
1 - 2 Years	£9,732,747.02	2.1%	£0.00	0.0%	£9,732,747.02	2.1%
2 - 5 Years	£39,648,657.81	8.6%	£0.00	0.0%	£39,648,657.81	8.5%
5 - 10 Years	£64,697,089.19	14.1%	£0.00	0.0%	£64,697,089.19	13.9%
10 - 20 Years	£141,933,076.58	30.8%	£0.00	0.0%	£141,933,076.58	30.5%
20 - 30 Years	£27,000,000.00	5.9%	£0.00	0.0%	£27,000,000.00	5.8%
30 - 40 Years	£109,000,000.00	23.7%	£0.00	0.0%	£109,000,000.00	23.4%
40 - 50 Years	£61,360,000.00	13.3%	£0.00	0.0%	£61,360,000.00	13.2%
> 50 Years	£0.00	0.0%	£0.00	0.0%	£0.00	0.0%
Total	**£460,398,695.41**	**100.0%**	**£5,000,000.00**	**100.0%**	**£465,398,695.41**	**100.0%**

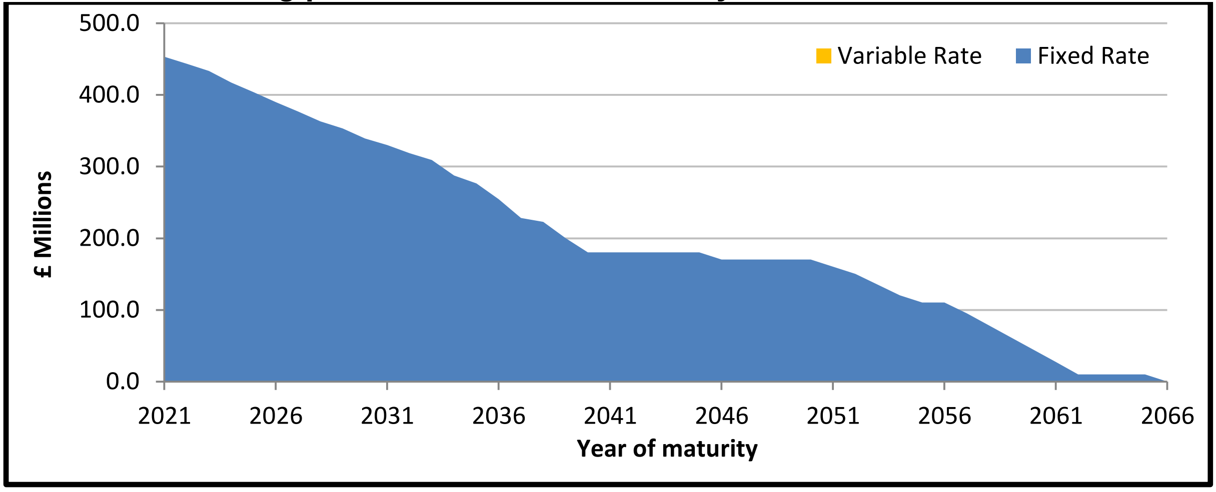
4.8. Chart 1 below shows the annual maturity profile of the Council's borrowing portfolio:

Chart 1: Borrowing profile at 31st March 2020 by annual maturities



4.9. Chart 2 below shows the fallout structure of the Council's borrowing portfolio:

Chart 2: Borrowing profile at 31st March 2020 by cumulative annual maturities



4.10. No new borrowing was undertaken during 2019/20. PWLB loan principal totalling £7.604m was repaid along with the final £6.500m of zero percent loans from Homes and Communities Agency as part of tariff arrangements, all in line with loan agreements. The average rate across the Council's borrowing portfolio at 31st March 2020 was 4.35% (from 4.37% on 31st March 2019).

4.11. The Council continues to hold a £5m Lender's Option Borrower's Option (LOBO) loan where the lender has the option every 6 months to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. Treasury management practice is to present such loans at their next potential maturity date (in this case a rolling 6 month exposure) rather than their backstop maturity date (in this case November 2041). Given underlying market conditions the lender did not exercise their option during 2019/20 and is not expected to do so in the near future, so officers are considering this loan to be long term funding.

5. Debt Restructuring

5.1. No debt rescheduling was undertaken during the year. Debt rescheduling opportunities have been limited due to the current economic climate and consequent structure of interest rates. Officers and the Councils treasury advisors continue to monitor this position.

6. HRA Debt Pooling arrangements

6.1. The 1st April 2012 saw the introduction of the Housing Self-Financing regime. As previously reported this Council adopted a single pool approach, whereby the Council manages its overall debt as a single portfolio and apportions costs to the General Fund and HRA at a consolidated rate in proportion to the debt held by each.

6.2. By adopting a single pool approach, any borrowing decisions by the General Fund impact upon the consolidated rate and therefore the debt costs apportioned to the HRA, and vice versa. As long as borrowing decisions are relatively balanced, then the impact is mitigated.

6.3. But on 30th October 2018, the Government removed the imposed debt caps which restricted how much housing authorities could borrow against their HRA. This opens up significant freedoms for additional borrowing by the HRA to support housing regeneration and new housing stock build programmes subject to the usual assessment criteria of the Prudential Code in demonstrating affordability, prudence and sustainability. In addition the Council would need to establish a clear metrics for assessing HRA debt that may include commercial costing measures such as capital risk buffers, debt interest cover ratios and loan-to-value limits.

6.4. This increased capacity for significant HRA borrowing means that the Council's single pool approach to managing debt may no longer be most appropriate, and the General Fund and HRA may be better suited pursuing separate debt strategies. Officers, in consultation with the Council's treasury advisors, are conducting a review of the debt pooling options available to the Council to establish the most suitable form of future debt management arrangements.

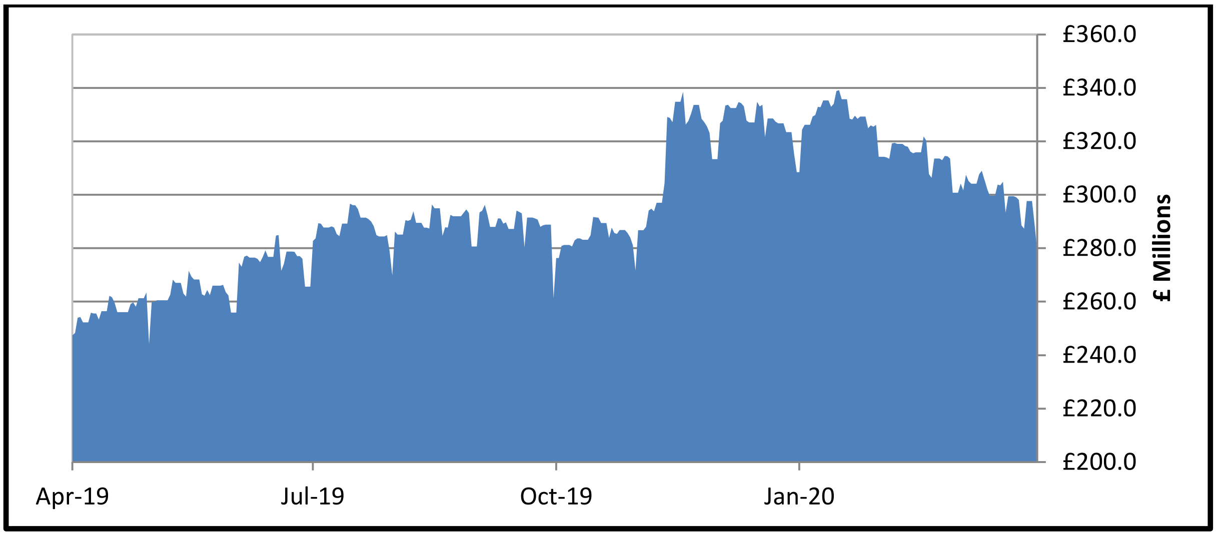
7. Investments

7.1. The Council's investment activity during the year conformed to the approved strategy, and the Council had no difficulties meeting its liquidity requirements.

7.2. The Council's investment portfolio represents the short-term holding of positive cashflows at any given time, plus prudent medium and long term provisions, balances and reserves.

7.3. During 2019/20, the Council's investment balances ranged from a low of £244.1m to a high of £339.2m due to timing differences between income and expenditure. The average balance held was £294.4m. Chart 3 below plots the 2019/20 annual cycle of fluctuation in investment balances:

Chart 3: Total Investment balances held during 2019/20



7.4. Table 3 below shows the Council's investment maturity position at 31st March 2020:

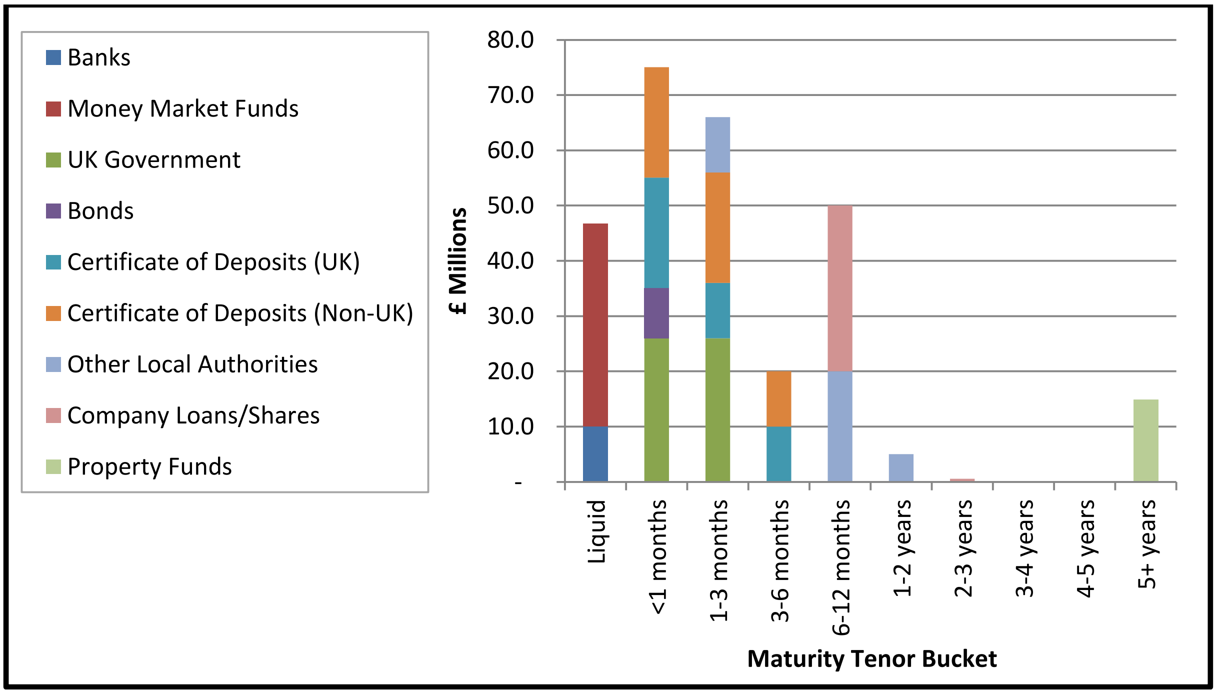
Table 3: Investment Maturity Position at 31st March 2020

Counterparty	Start Date	Maturity Date	Interest Rate	Interest Rate Structure	Principal O/S (£)
Same-day access: Banks					
Barclays Bank plc	n/a	n/a	0.0000%	Variable	15,004.13
National Westminster Bank plc	n/a	n/a	0.3000%	Variable	10,001,150.71
					10,016,154.84
Same-day access: Money Market Funds					
Deutsche	n/a	n/a	0.4044%	Variable	100,000.00
Federated	n/a	n/a	0.4250%	Variable	100,000.00
Aberdeen	n/a	n/a	0.4694%	Variable	100,000.00
Legal and General Investment Management	n/a	n/a	0.4019%	Variable	100,000.00
Insight	n/a	n/a	0.2749%	Variable	15,000,000.00
Morgan Stanley	n/a	n/a	0.3307%	Variable	10,255,000.00
State Street Global Advisors	n/a	n/a	0.3827%	Variable	100,000.00
Goldman Sachs	n/a	n/a	0.2707%	Variable	10,925,000.00
					36,680,000.00
UK Government:					
Debt Management Office	09/01/20	09/04/20	0.6800%	Fixed	26,000,000.00
Debt Management Office	07/02/20	07/05/20	0.6700%	Fixed	26,000,000.00
					52,000,000.00
Bonds: UK					
HSBC Bank UK plc	15/11/19	14/04/20	0.7550%	Fixed	5,981,317.80
HSBC Bank UK plc	14/10/19	14/04/20	0.7901%	Fixed	3,087,767.45
					9,069,085.25
Certificate of Deposits: UK					
Lloyds Bank plc	17/10/19	17/04/20	0.8800%	Fixed	10,000,000.00
Standard Chartered Bank	17/10/19	17/04/20	0.8100%	Fixed	10,000,000.00
Nationwide Building Society	15/11/19	15/05/20	0.8300%	Fixed	10,000,000.00
Santander UK plc	17/01/20	17/07/20	0.7300%	Fixed	10,000,000.00
					40,000,000.00
Certificate of Deposits: Non-UK					
Nordea Bank AB (Finland)	17/10/19	17/04/20	0.8100%	Fixed	10,000,000.00
Toronto Dominion Bank (Canada)	17/10/19	17/04/20	0.7900%	Fixed	10,000,000.00
DZ Bank (Germany)	15/11/19	15/05/20	0.8300%	Fixed	10,000,000.00
Rabobank (Netherlands)	17/12/19	17/06/20	0.7200%	Fixed	10,000,000.00
Landesbank Baden-Wuerttemberg (Germany)	17/01/20	17/07/20	0.7100%	Fixed	10,000,000.00
					50,000,000.00
Other Local Authorities:					
Wirral Metropolitan Borough Council	25/03/20	25/06/20	1.6500%	Fixed	5,000,000.00

Counterparty	Start Date	Maturity Date	Interest Rate	Interest Rate Structure	Principal O/S (£)
Southampton City Council	25/03/20	25/06/20	2.0000%	Fixed	5,000,000.00
Folkestone and Hythe District	25/03/20	25/03/21	1.6500%	Fixed	5,000,000.00
South Somerset District Council	27/03/20	26/03/21	1.6000%	Fixed	5,000,000.00
Telford and Wrekin Borough Council	25/03/20	31/03/21	1.6500%	Fixed	5,000,000.00
Armagh City Banbridge and Craigavon Borough Council	27/03/20	31/03/21	1.6000%	Fixed	1,000,000.00
Gwynedd County Council	30/03/20	31/03/21	1.6000%	Fixed	4,000,000.00
Cheshire West and Chester Council	31/03/20	31/03/22	1.8000%	Fixed	5,000,000.00
					35,000,000.00
Company Loans/Shares:					
Milton Keynes Development Partnership LLP	12/11/19	12/11/20	2.7700%	Fixed	30,000,000.00
YourMK LLP (shares)	09/08/16	n/a	0.0000%	Fixed	100.00
YourMK LLP	09/08/16	09/08/22	3.8116%	Variable	550,726.19
					30,550,826.19
Property Funds (variable net asset value [VNAV]):					
CCLA Local Authorities Property Fund	30/03/15		4.3038%	Variable	10,121,148.47
CCLA Local Authorities Property Fund	26/02/16		4.3038%	Variable	4,758,947.53
					14,880,096.00
					278,196,162.28

7.5. Chart 3 below shows the investment portfolio maturity profile by tenor buckets per category type at 31st March 2020:

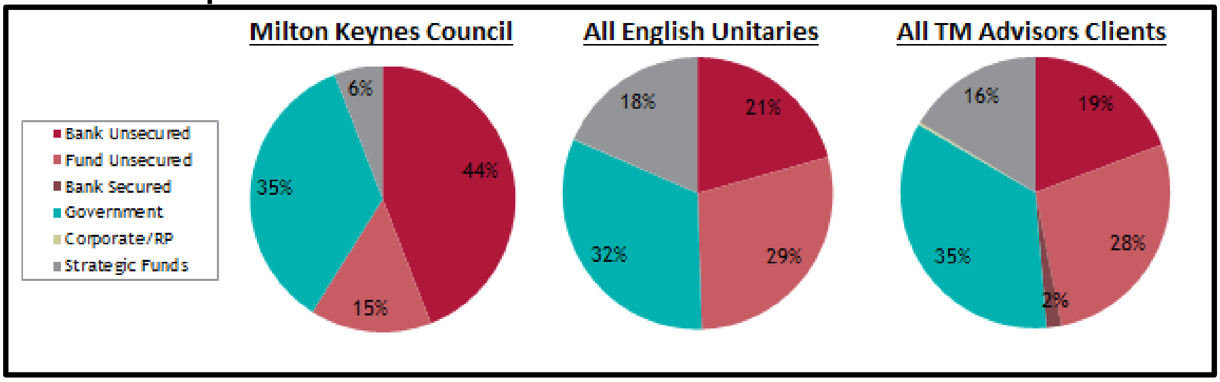
Chart 3: Investment profile at 31st March 2020 by maturity category & tenor buckets



7.6. Investment balances bought forward at 31st March 2019 were £235.862m. Due to the front-loaded nature of various government funding streams, the average level of funds available for investment purposes during the year was £294.366m (£237.336m for 2018/19). As shown in Table 3 above, actual balances at 31st March 2020 were £278.196m, primarily due to delays & rephrasing of the capital programme.

7.7. Chart 4 below shows the composition of the Council's investment portfolio by risk exposure, against other English unitary authorities and the Council's treasury advisors client base.

Chart 4: Composition of Investment Portfolio



Externally managed strategic funds:

7.8. The Council has invested a total of £15m into an externally managed strategic pooled property fund with the CCLA; £10m in March 2015 and a further £5m in February 2016. Short-term security and liquidity are lesser considerations for this type of investment with the primary objectives instead being regular revenue income and long-term price stability. This fund generated a £0.658m net income return towards supporting public services.

7.9. At 31st March 2019, the fair value of the Council's holdings was £15.594m. At 31st March 2020, the fair value of the Council's holdings had decreased to £15.042m, representing a £0.552m fall in value. Excluding accrued interest of £0.162m, the fair value at 31st March 20 is £0.120m lower than the Councils initial £15.0m cash investments, which represents an unrealised loss at the 31st March 20 held in the Available for Sale Financial Instruments Reserve. The Council has no plans to liquidate this investment.

7.10. CCLA issued a notice on 25th March 2020 to suspend purchase and redemption transactions in direct response to the pervasive effects of Covid-19 (coronavirus). Sharp falls in economic activity and the relative infrequency of transactions in the property sector means that it is not possible for the CCLA's valuers to be confident that their valuations will truly reflect prevailing conditions at this time. The CCLA has a duty to ensure that all transactions in the property fund are conducted at prices which are accurate and fair to both shareholders and those wishing to purchase or sell units/shares. In circumstances where that is not possible, and where there is therefore a material risk of disadvantage to either party, the CCLA are obliged to suspend transactions until the required level of certainty can be re-established.

7.11. The temporary suspension of the CCLA Property Fund does not have an immediate or significant impact on the Council, which has always been treated its holdings as a long term strategic investment. During the period of suspension, the Council will continue to receive dividend returns as normal.

7.12. Officers took part in a briefing session with the CCLA fund management team in April 2020. The fund is effectively entering this period of global crisis from the impact of COVID-19 from a well-managed base risk position on back of over a decade of market instability since the 2008 financial crisis, as well as the more recent and continuing heightened risks surrounding Brexit.

7.13. The CCLA takes a distinct approach to its asset acquisitions in that it does not buy assets simply for short-term gain, but a diversified range of long-term and adaptable assets that could, in most cases, be repurposed. Evidence so far suggests the current impact upon commercial property markets is contained and focused on those already underperforming specific sub-categories like, high street retail. The reality is that retail markets were evolving this way beforehand, and this crisis has simply accelerated those trends. Other than housing, there is high demand for long-term commercial warehousing as well as flexible multi-purpose office spaces.

7.14. Officers will continue to monitor the performance of the CCLA property fund investment.

Investments for policy reasons outside of normal treasury management operations:

7.15. Although not classed as treasury management activities per se, the 2017 CIPFA Code now requires the Council to report on investments for policy reasons outside of normal treasury management operations. This includes service investments for operational and/or regeneration as well as commercial investments made primarily for financial income reasons. These investments typically earn a higher rate of return compared to normal treasury management investments, which reflects the additional risks that the Council is exposed to.

7.16. During 2019/20 the Council renegotiated a £30.0m 1-year loan to its wholly owned subsidiary company Milton Keynes Development Partnership (MKDP) LLP, used to finance the acquisition of assets from the Homes and Communities Agency (HCA) in 2012/13. The loan rate of 2.77% was set with reference to State Aid regulations and prevailing market rates.

7.17. The Council has lent £0.5m in tranche payments to its 50% joint-owned partnership company YourMK LLP. YourMK is a partnership between the Council and Mears Group to deliver regeneration, management of council housing stock, and other development on council land and it is responsible for all Housing Land under the Council. At 31st March 2020, the Council's investment holding was valued at £0.551m, of which £0.051m represents an unrealised gain through accruing compound interest since advanced. During 2019/20, this investment generated £0.021m of interest income for the Council at an average rate of return of 3.96%.

7.18. The Council holds a £5.0m principal investment (match-funded by external investment) in a National Homelessness Property Fund, the assets of which are for use as housing temporary accommodation in Milton Keynes. At 31st December 2019 (latest available) the Net Asset Value of the Council's investment was £4.488m, which represents an unrealised revaluation loss against principal of £0.512m. The valuation loss is due to basis of asset valuation; assets were acquired on an Open Market Value (OMV) basis but have been revalued at Existing Use Value (EUV) based on sub-market rental income streams due to ongoing use as temporary accommodation. If those assets were sold to liquidise the Council's investment, it would expect to be with vacant possession and the valuation method would revert to OMV and so it is anticipated that the book loss would be fully recovered. This investment generated £0.104m of investment income for the Council, representing a rate of return of 2.08%. This investment is not shown within the tables and charts above as it was funded through the capital programme and reported through the capital monitoring process.

8. Investment income performance:

8.1. The Council's investments income return for 2019/20 exceeded the budget expectation. Projections for the financial year are reported through the Budget Monitoring process and the final position for the year through the Budget Monitoring Outturn report.

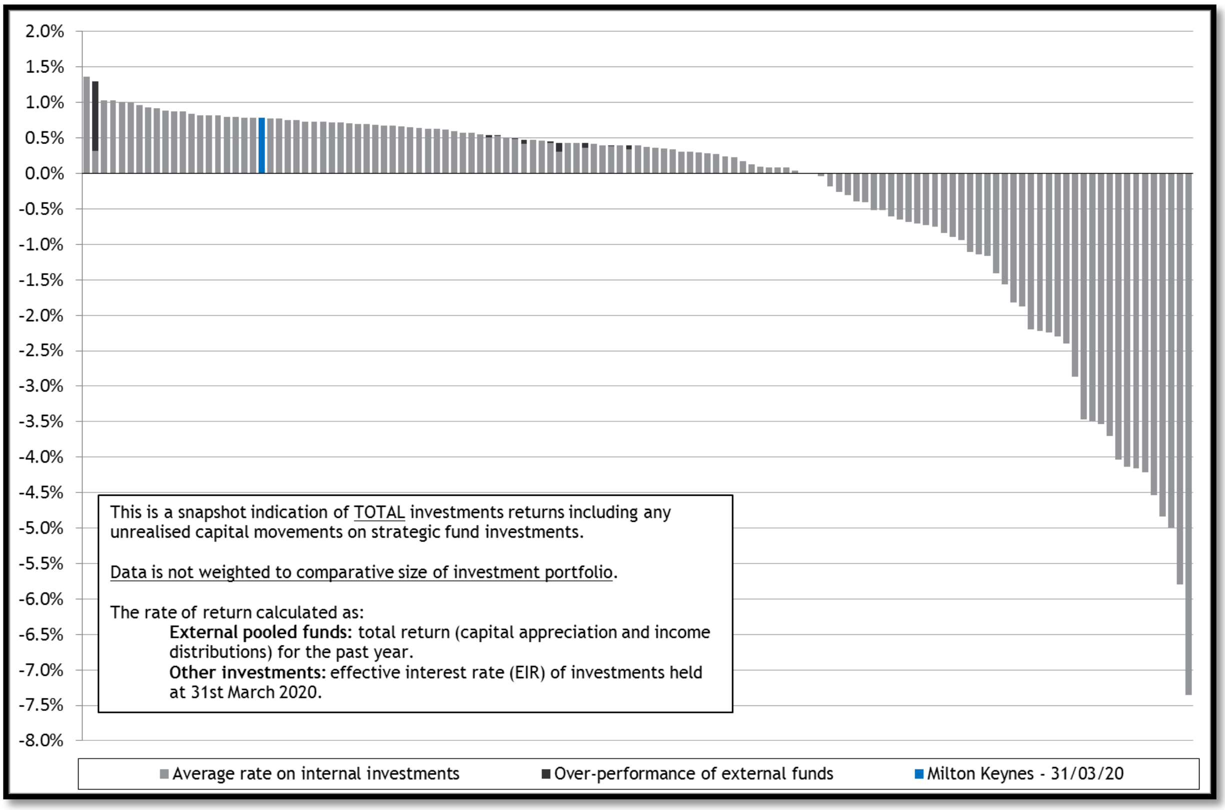
8.2. Investment income performance against the 3 month London Interbank Bid Rate (LIBID), which is the bidding rate at which banks are willing to borrow from each other, is shown in Table 4 below:

Table 4: Investment income performance against 3 month LIBID benchmark

Period	MKC Performance	Benchmark Performance	Difference
Q1 (Apr-Jun)	1.03%	0.76%	+0.27%
Q2 (Jul-Sept)	0.97%	0.71%	+0.26%
Mid Year Average (Apr-Sept)	**1.00%**	**0.75%**	**+0.25%**
Q3 (Oct-Dec)	0.92%	0.67%	+0.25%
Q4 (Jan-Mar)	1.05%	0.55%	+0.50%
Annual Average (Apr-Mar)	**1.00%**	**0.63%**	**+0.37%**

8.3. Chart 5 below shows the Council's total investment return - that is the income return stated in Table 4 above from investments net of any <u>unrealised</u> gains or losses on strategic funds – compared to the Council's treasury advisors client base. This illustrates that the Council's performance is in the top quartile and has been shielded from large scale devaluation of strategic fund assets suffered by some authorities. Note that this is a snapshot indication and data is not weighted to comparative size of investment portfolio.

Chart 5: 2019/20 total investment returns across TM advisors client base



9. Compliance with Treasury and Prudential Limits

9.1. It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators are set as part of the Treasury Management Strategy and Capital Strategy.

9.2. During the financial year the Council has operated within its treasury limits and Prudential Indicators.

9.3. The Prudential and Treasury Indicators are shown in Table 5 below.

Table 5: Prudential and Treasury Indicators

Prudential Indicator		**2019/20 Indicator**	**2019/20 Actual ***
Authorised limit for external debt		----- £755.000m -----	
Operational boundary for external debt		----- £725.000m -----	
Gross borrowing		£465.398m	£465.399m
Capital Financing Requirement (CFR)		£697.315m	£714.007m
Ratio of financing costs to net revenue streams:	GF	10.11%	9.84%
	HRA	38.03%	37.65%
Limit of fixed interest rates based on net debt		£715.000m	£244.330m
Limit of variable interest rates based on net debt		£30.000m	-£57.127m
Principal sums invested > 365 days		£50.000m	£20.431m
Maturity structure of borrowing limits:-			
Under 12 months		Max. 15% Min. 0%	2.6%
12 months to 2 years		Max. 15% Min. 0%	2.1%
2 years to 5 years		Max. 50% Min. 0%	8.5%
5 years to 10 years		Max. 50% Min. 0%	13.9%
10 years and above		Max. 100% Min. 50%	72.9%

* subject to revision at final outturn.