APPENDIX 1

Lewes District Council

Annual Treasury Management Report 2019/20

Contents

1. Background

1.1 The Council is required through regulations issued under the Local Government Act 2003 to produce an annual treasury management report. The report must review treasury management activities and set out the final position of the Council's Treasury Prudential Indicators. This report meets the requirements of both the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities.

1.2 The Council defines its Treasury Management activities as:

"the management of the Council's 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 The Council agreed its Treasury Management Strategy Statement and Investment Strategy 2019/20 to 2021/22 at its meeting in February 2019. The Council has substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remain central to the Council's treasury management strategy.

1.4 The 2017 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy, complying

2. Overall Summary of Activity 2019/20

2.1 The table below lists the key elements of the 2019/20 Strategy and records actual performance against each one of them.

Key Element	Target in Strategy	Actual Performance	
Borrowing			
Underlying need to borrow (CFR) at year end	£87.100 million	£85.424 million	-
Internal borrowing at year end	£30.427 million	£28.751 million	-
New external long-term borrowing in year	None anticipated	None undertaken	✓
Debt rescheduling in year	Review options but not anticipated	Options kept under review, none undertaken	✓
Interest payments on external borrowing	£1.7 million	£1.745 million	✓
Investments			
Minimum counterparty credit ratings for unsecured investments	Long-term BBB+- (does not apply to Government and other local authorities which have the highest ratings)	At least Long-term A	✓
Interest receipts from external investments	£0.100m	£0.107 m	✓

Key Element	Target in Strategy	Actual Performance	
Appointment of Investment Consultants			
Independent Treasury Adviser to be retained	Arlingclose to be retained as Treasury Adviser	Arlingclose retained as Treasury Adviser	✓
Reporting and Training			
Reports to be made to Audit and Standards Committee and Cabinet	Every regular meeting	Every regular meeting.	✓
Briefing sessions for Councillors and Staff	Treasury Adviser to provide	Staff training September 2019	✓

2.2 The remainder of this report explores each of the key elements in more depth. Appendix A gives details of the final position on each of the Prudential Indicators, and Appendix B explores the Economic Background to the year's activity. A glossary appears at the end of the document to explain technical terms which could not be avoided when writing this report.

3. Detailed Analysis – Borrowing

3.1 On 9th October 2019 the PWLB raised the cost of certainty rate borrowing by 1% to 1.8% above UK gilt yields as HM Treasury was concerned about the overall level of local authority debt. PWLB borrowing remains available but the margin of 180bp above gilt yields appears relatively very expensive. Market alternatives are available and new products will be developed; however, the financial strength of individual authorities will be scrutinised by investors and commercial lenders.

3.2 The Chancellor's March 2020 Budget statement included significant changes to Public Works Loan Board (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, available from 12 March 2020 and £1.15bn of additional "infrastructure rate" funding at gilt yields plus 0.60% to support specific local authority infrastructure projects for England for which there is a bidding process.

3.3 Other than for temporary cash flow purposes, local authorities are only allowed to borrow to finance capital expenditure (e.g. the purchase of property, vehicles or equipment which will last for more than one year, or the improvement of such assets). Prior to 2018/19, the Government limited the amount of borrowing by local authorities for housing purposes by specifying 'debt caps'. The Council's underlying debt cap was fixed at £72.931m. Previously, local authorities were able to bid for an increase in the housing debt cap in order to enable specific projects. A bid from the Council was successful and the debt cap was increased to £75.248m to match expenditure incurred in building new houses on specified former garage sites. The Government removed the 'debt cap' during 2018/19, which enables the Council to further invest in the provision of new social housing.

3.4 In accounting terms, the underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR) while usable reserves and working capital are the underlying resources available for investment.

3.5 The CFR is, in simple terms, the amount of capital expenditure which has been incurred by the Council but which has not yet been paid for (by using, for example, grants, capital receipts, reserves or revenue income) and in the meantime is covered by internal or external borrowing. 'External borrowing' is where loans are raised from the Public Works Loans Board (PWLB) or banks. Alternatively it is possible to 'internally borrow' the significant levels of cash which has been set aside in Balances and Reserves and which would otherwise need to be invested with banks or other counterparties.

3.6 As noted above, the level of CFR increases each year by the amount of unfinanced capital expenditure and is reduced by the amount that the Council sets aside for the repayment of borrowing. The original CFR projection for 2019/20, the revised position reported at the time of producing the Treasury Strategy 2020/21 (February 2020) and the final position for the year are shown in the table below. The variation between the revised and final position reflects the changing profile of capital spend across financial years, particularly allocations in the capital programme in respect of facilitating loans to Lewes Housing investment Company, and Aspiration Homes LLP.

3.7

	2019/20 Original	2019/20 Revised	2019/20 Outturn
	£m	£m	£m
Opening CFR	133.079	82.030	82.030
Capital expenditure in year	11.900	15.000	14.197
Less financed	(7.700)	(9.618)	(10.511)
Less amount set aside for debt repayment	(0.292)	(0.312)	(0.292)
Closing CFR	**136.987**	**87.100**	**85.424**

3.8 The overall CFR can be split between the General Fund and the Housing Revenue Account as follows:

	2019/20 Revised	2019/20 Outturn
CFR Component	£m	£m
General Fund	21.100	18.077
Housing Revenue Account	66.000	67.347
Total	**87.100**	**85,424**

3.9 The following table compares the CFR with the amount that the Council holds in balances and reserves as well as working capital (day to day cash movements as well as grants, developer contributions and capital receipts held, pending their use).

	31/3/20 Revised £m	31/3/20 Outturn £m
(a) Capital Financing Requirement	87.100	85.424
(b) Actual external long-term borrowing	(56.673)	(56.673)
(c) Borrowing required in year	-	-
(d) Use of Balances and Reserves and working capital as alternative to borrowing (a)–(b)-(c)	30.427	28,751

3.10 The Council's long-term loan portfolio at 31 March 2020 was:

Lender	Interest	Amount £m	Rate %	Maturity
PWLB	Fixed	4.000	2.70	01-03-2024
PWLB	Fixed	5.000	3.30	01-03-2032
PWLB	Fixed	2.000	3.05	01-09-2027
PWLB	Fixed	2.000	2.76	01-09-2024
PWLB	Fixed	4.000	2.97	01-09-2026
PWLB	Fixed	5.000	3.28	01-09-2031
PWLB	Fixed	4.000	2.63	01-09-2023
PWLB	Fixed	5.000	3.44	01-03-2037
PWLB	Fixed	6.673	3.50	01-03-2042
PWLB	Fixed	5.000	3.43	01-09-2036
PWLB	Variable	5.000	0.88	28-03-2022
PWLB	Fixed	4.000	3.01	01-03-2027
	Sub-total	**51,673**		
Barclays	Fixed	5.000	4.50	06-04-2054
	Sub-total	**5.000**		
	Total	**56.673**		

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

3.12 In the table above the Barclays loan was taken out in April 2004 with a term of 50 years. In June 2016 the bank decided to permanently waive its contractual right to vary the interest rate on this loan, which was effectively fixed at the rate of interest applicable at that time, 4.5%.

3.13 Total interest paid on external long-term borrowing in the year was £1.745m, which was consistent with the revised budget for the year. No new long-term borrowing was undertaken. The Council remained eligible to access the Government's 'Certainty Rate' allowing the Council to borrow, had it been appropriate to do so, at a reduction of 0.2% on the Standard Rate.

3.14 Through the year, officers, supported by Arlingclose, monitored opportunities for the rescheduling of external loans and the possibility of repayment utilising cash balances that would otherwise be invested. No beneficial rescheduling opportunities were identified and the loan portfolio remained unchanged through the year.

3.15 As determined by the Council, two separate Loans Pools operated in 2019/20, for the General Fund and HRA respectively. At 31 March 2020 the balance on internal loans from the General Fund to the Housing Revenue Account (HRA) was £8.795m, an increase of £0.264m compared with the previous year, which comprised new lending as funding for the construction of new homes. Interest was charged on internal borrowing at 1.66% (equivalent to a one-year maturity loan from the PWLB at the start of the financial year).

3.16 No temporary borrowing was undertaken during the course of the financial year and consequently, there were no temporary loans outstanding at 31 March 2020.

4. Detailed Analysis - Investments

4.1 In a relatively short period since the onset of the COVID-19 pandemic, the global economic fallout was sharp and large. Market reaction was extreme with large falls in equities, corporate bond markets and, to some extent, real estate echoing lockdown-induced paralysis and the uncharted challenges for governments, businesses and individuals. Volatility measured by the VIX index was almost as high as during the global financial crisis of 2008/9 and evidenced in plummeting equity prices and the widening of corporate bond spreads, very close to rivalling those twelve years ago. Gilt yields fell but credit spreads widened markedly reflecting the sharp deterioration in economic and credit conditions associated with a sudden stagnation in economies, so corporate bonds yields (comprised of the gilt yield plus the credit spread) rose and prices therefore fell.

4.2 The Council held an average of £17m as cash during the year. This comprised working cash balances, capital receipts, earmarked reserves and developer contributions held pending their use.

4.3 The Council's general policy objective is to invest its surplus funds prudently. Throughout 2019/20, the Council's investment priorities continued to be:

Highest priority - Security of the invested capital;
Followed by - Liquidity of the invested capital;
Finally - An optimum yield commensurate with security and liquidity.

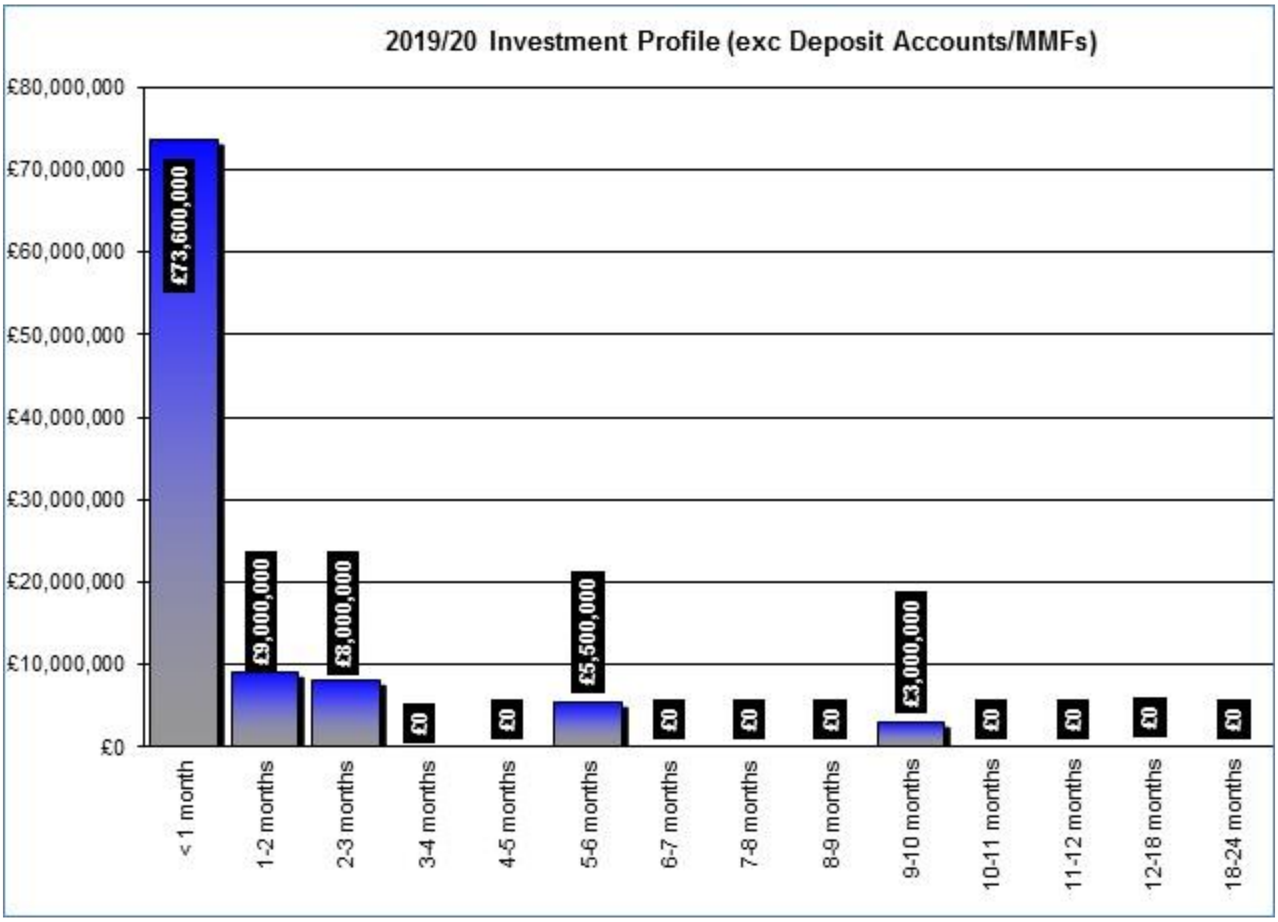
4.4 All of the Council's investments were managed in-house. Security of capital was maintained by following the counterparty policy set out in the Investment Strategy for 2019/20. Investments made during the year included:

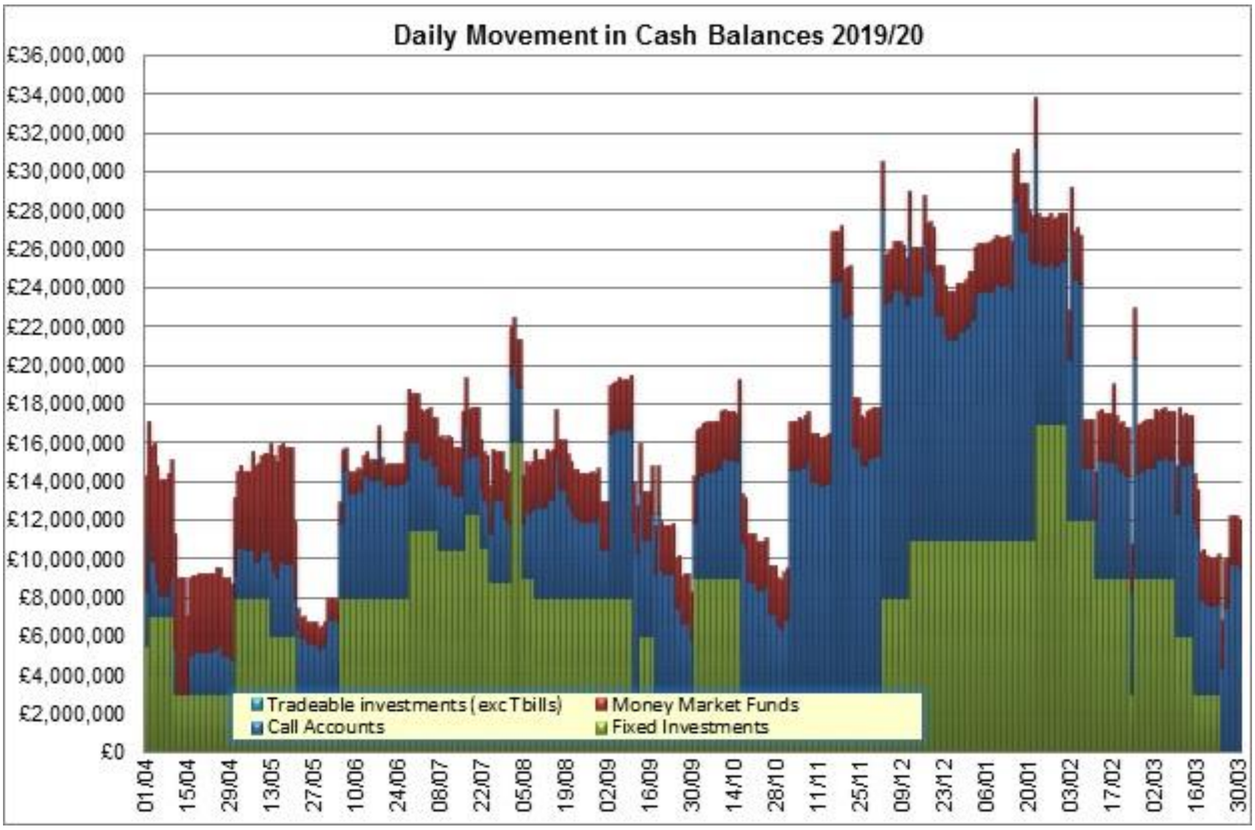
- Fixed Term Deposits with the Debt Management Office (DMO) (a total of £67.6 million – 14 occasions);
- Fixed Term Deposits with other Local Authorities (a total of £26 million – 7 occasions);
- Fixed Term Deposits with UK Banks and Building Societies (none);
- Investments in Money Market Funds (MMFs) (average daily balance held in year £1.35 million);
- United Kingdom Treasury Bills (none);
- Tradable Investments - Floating Rate Notes, Certificates of Deposit, Bonds (none);
- Deposit accounts with UK Banks (average daily balance held in year £2.23 million);
- Deposit accounts with UK Building Societies (none);
- Overnight deposits with the Council's banker, Lloyds Bank (average daily balance held in year £4.6 million).

4.5 Counterparty credit quality was assessed and monitored with reference to credit ratings (a minimum long-term counterparty rating of BBB+ across all three rating agencies Fitch, Standard and Poor's, and Moody's applied); credit default swaps; GDP of the country in which the institution operates; the country's net debt as a percentage of GDP; any potential support mechanisms and share price.

4.6 In keeping with Government guidance on investments, the Council maintained a sufficient level of liquidity through the use of Money Market Funds (MMF), overnight deposits and deposit accounts, the average daily balance held being £9.53million.

4.7 A full list of investments (excluding deposit account or MMF transactions) made or maturing in the year is given at Appendix C. All investments were made with UK institutions, and no new deposits were made for periods in excess of one year. The first chart below gives an analysis of aggregate fixed term deposits by duration. The second chart shows how the total amount invested varied from day to day over the course of the year, from a low of £6.4m to a high of £31.1m. The movement largely reflects the cycle of grant, council tax and business rate receipts and precept payments made.





4.8 The income return generated from investments in the year was £0.107 million, above the total budget for investment income of £0.100 million. This position arose as a result of the requirement to re-profile major projects within the approved capital programme, ensuring an increase in the short-term availability of additional cash for investment.

4.9 The average rate of return from investments at the end of each quarter in 2019/20 is shown in the table below, along with comparative benchmark information, the 7-day LIBID rate.

Average rate of investments in:	Lewes District Council	7 day LIBID
Quarter 1 ending 30 June 2019	0.77%	0.57%
Quarter 2 ending 30 September 2019	0.66%	0.56%
Quarter 3 ending 31 December 2019	0.51%	0.57%
Quarter 4 ending 31 March 2020	0.48%	0.43%
Whole year 2019/20	0.61%	0.53%

5. Compliance with Prudential Indicators

5.1 The Council can confirm that it has complied with its Prudential Indicators for 2019/20. A detailed review of each of the Prudential Indicators is at Appendix A.

6. Investment Consultants

6.1 The Council appointed Arlingclose as its Treasury Adviser in 2012 following an open procurement. The agreement with Arlingclose was for an initial four- year term expiring on 30 June 2016, with the Council having the option to extend for a further year.

6.2 The Council exercised the option to extend the agreement to the end of June 2017 and following discussion with Arlingclose opted to maintain the appointment for a further year. A further treasury management adviser services for both Councils have been reviewed and the Link Market Services has been appointed to support both the Lewes District Council and Eastbourne Borough Council, given that a shared finance team (with treasury management responsibility) has been established.

7. Reporting and Training

7.1 The Chief Finance Officer reported the details of treasury management activity to each regular meeting of the Audit and Standards Committee and Cabinet held in 2019/20. A mid-term summary report was issued in November 2019.

7.2 The training needs of the Council's treasury management staff were reviewed as part of the annual corporate staff appraisal/training needs assessment process for all Council employees. Members of staff attended, where appropriate, Arlingclose workshops alongside colleagues from other local authorities during 2019/20.

7.3 In 2019/20, Arlingclose met with Council officers with a role in treasury management both to explain developments within the sector, as well as review the Council's own investment and debt portfolios.

7.4 The Treasury Strategy had anticipated that Arlingclose would hold a local briefing session for all councillors tasked with treasury management responsibility, including scrutiny of the treasury management function. The TM briefing session took place in September 2019.

Appendix A – Prudential Indicators 2019/20

1. Background:

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators. Some of the Prudential Indicators relate directly to the Council's Capital Programme. These Indicators are also included below for completeness of reporting.

2. Net Borrowing and the Capital Financing Requirement

2.1 This is a key indicator of prudence. In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that the net external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

2.2 The Chief Finance Officer reports that the Council has had no difficulty meeting this requirement in 2019/20, nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the budget for 2020/21.

3. Estimates of Capital Expenditure (direct link to Capital Programme)

This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax and in the case of the HRA, housing rent levels.

No.	Capital Expenditure	2019/20 Original £m	2019/20 Revised £m	2019/20 Actual £m
1a	Non-HRA	6.900	8.000	7.486
1b	HRA	5.000	7.000	6.711
	Total	**11.900**	**15.000**	**14.197**

4. Ratio of Financing Costs to Net Revenue Stream (direct link to Capital Programme)

4.1 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs.

4.2 The ratio is based on costs net of investment income. Where investment income exceeds interest payments, the indicator is negative.

No.	Ratio of Financing Costs to Net Revenue Stream	2019/20 Original %	2019/20 Revised %	2019/20 Actual %
2a	Non-HRA	1.68	2.00	1.55
2b	HRA	18.08	13.20	11.51

5. Capital Financing Requirement

5.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and it's financing. The amounts shown are as at 31 March.

No	Capital Financing Requirement	2019/20 Original £m	2019/20 Revised £m	2019/20 Actual £m
3a	Non-HRA	69.268	21.100	18.077
3b	HRA	67.719	66.000	67.347
	Total CFR	**136.987**	**87.100**	**85.424**

5.2 The year-on-year change in the CFR is set out below.

Capital Financing Requirement	2019/20 Original £m	2019/20 Revised £m	2019/20 Actual £m
Balance B/F	133.079	82.030	82.030
Capital expenditure financed from borrowing	4.200	5.382	3.686
Revenue provision for Debt Redemption.	(0.292)	(0.312)	(0.292)
Balance C/F	**136.987**	**87.100**	**85.424**

6. Actual External Debt

This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities. The Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit (see 8 below).

No.	Actual External Debt as at 31/03/20	Revised £m	Actual £m
4a	Borrowing	127.305	56.673
4b	Other Long-term Liabilities	0.392	0.144
4c	**Total**	**127.797**	**56.817**

7. Incremental Impact of Capital Investment Decisions Stream (direct link to Capital Programme)

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and Housing Rent levels. The incremental impact is calculated by comparing the total revenue budget requirement of the current approved Capital Programme with an equivalent calculation of the revenue budget requirement arising from the proposed Capital Programme.

No.	Incremental Impact of Capital Investment Decisions	2019/20 Original £	2019/20 Revised £	2019/20 Actual £
5a	Increase in Band D Council Tax	64.74	50.33	34.52
5b	Increase in Average Weekly Housing Rents	0.78	0.75	0.84

The increase in Band D council tax/average weekly rents reflects the funding of the capital programme: for example, new borrowing increases interest payable, and funding from reserves utilises resources which could have otherwise been used to fund revenue expenditure. The actual indicators are less than the revised as a result of significant capital projects being deferred from 2019/20 into 2020/21.

8. Authorised Limit and Operational Boundary for External Debt

8.1 The Council has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise as a consequence of all the financial transactions of the Council and not just those arising from capital spending reflected in the CFR.

8.2 The Authorised Limit sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities). This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases.

8.3 The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements.

8.4 The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit). The 2019/20 Actual values shown below are the maximum levels of borrowing, including temporary borrowing, experienced at any time during the year.

No.	Authorised Limit for External Debt	2019/20 Original £m	2019/20 Revised £m	2019/20 Actual £m
6a	Borrowing	127.308	127.305	56.673
6b	Other Long-term Liabilities	0.392	0.392	0.144
6c	**Total**	**127.700**	**127.797**	**56.817**

8.5 The Operational Boundary links directly to the Council's estimates of the CFR and estimates of other cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

8.6 The Chief Finance Officer has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next meeting of the Cabinet. The 2019/20 Actual values shown below are the maximum levels of borrowing, including temporary borrowing, experienced at any time during the year.

No.	Operational Boundary for External Debt	2019/20 Original £m	2019/20 Revised £m	2019/20 Actual £m
7a	Borrowing	111.300	116.908	56.673
7b	Other Long-term Liabilities	0.392	0.392	0.144
7c	**Total**	**111.692**	**117.300**	**56.817**

9. Adoption of the CIPFA Treasury Management Code

This indicator demonstrates that the Council has adopted best practice.

No.	Adoption of the CIPFA Code of Practice in Treasury Management
8	The Council approved the adoption of the CIPFA Treasury Management Code in 2002. Following revisions to the Code published in December 2009, reconfirmed its adoption of the Code in February 2010.

10. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

10.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. This Council calculates these limits on net principal outstanding sums i.e. fixed rate debt net of fixed rate investments.

10.2 The upper limit for variable rate exposure has been set to ensure that the Council is not exposed to interest rate rises which could adversely impact on the revenue budget.

No.		2019/20 Original £m	2019/20 Revised £m	2019/20 Actual £m
9	**Upper Limit for Fixed Interest Rate Exposure**	100.0	100.0	100.0
10	**Upper Limit for Variable Interest Rate Exposure**	(25)	(25.0)	(25.0)

10.3 The limits above provide the necessary flexibility within which decisions will be made for drawing down new loans on a fixed or variable rate basis; the decisions will ultimately be determined by expectations of anticipated interest rate movements as set out in the Council's Treasury Management Strategy.

10.4 Because the Council's investments are substantially in excess of its variable rate borrowing, the Upper Limit for Variable Interest Rate exposure is shown as a negative figure.

11. Maturity Structure of Fixed Rate borrowing

11.1 This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

11.2 It is calculated as the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate. The maturity of borrowing is determined by reference to the earliest date on which the lender can require payment.

No.	Maturity structure of fixed rate borrowing	Lower Limit %	Upper Limit %	Actual %
11a	under 12 months	0	75	0
11b	12 months and within 24 months	0	75	0
11c	24 months and within 5 years	0	75	18
11d	5 years and within 10 years	0	100	18
11e	10 years and above	0	100	56

12. Upper Limit for total principal sums invested over 364 days

The purpose of this limit is to contain exposure to the possibility of loss that may arise as a result of the Council having to seek early repayment of the sums invested. No investments of more than 364 days were made during 2019/20.

No.	Upper Limit for total principal sums invested over 364 days	2019/20 Original £m	2019/20 Revised £m	2019/20 Actual £m
12	Upper limit	2	2	2

13. HRA Limit on Indebtedness

The indicator is associated with self-financing for housing. It indicates the residual capacity to borrow for housing purposes, while remaining within the overall HRA 'Debt Cap' specified by the Government. The Government removed the 'debt cap' during 2019/20. The Council has retained the indicator 2019/20 for reporting to show the position if the 'debt cap' had remained in place.

No	Capital Financing Requirement	2019/20 Original £m	2019/20 Revised £m	2019/20 Actual £m
13a	HRA CFR	67.719	66.000	67.347
13b	HRA Debt Cap	75.248	75.248	75.248
	Difference	**7.529**	**9.248**	**7.901**

Appendix B – Economic Background explained by Arlingclose

Economic background: 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. Politics 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 confidence and activity.

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.

GDP growth in Q4 2019 was reported as flat by the Office for National Statistics 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%. 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 as part of a flight to quality into sovereign debt and other perceived 'safe' assets.

In response to the spread of the virus and sharp increase in those infected, the government enforced lockdowns, central banks and governments 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.

The Bank of England, 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 0.1%. In conjunction with these cuts, the UK government introduced a number of measures to help businesses and households impacted by a series of ever-tightening social restrictions, culminating in pretty much the entire lockdown of the UK.

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. 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: Financial markets sold off sharply as the impact from the coronavirus worsened. After starting positively in 2020, the FTSE 100 fell over 30% at its worst point with stock markets in other countries seeing similar huge falls. In March sterling touch its lowest level against the dollar since 1985. The measures implemented by central banks and governments helped restore some confidence and financial markets have rebounded in recent weeks but remain extremely volatile. The flight to quality caused gilts yields to fall substantially. The 5-year benchmark fell from 0.75% in April 2019, to 0.26% on 31st March. The 10-year benchmark yield fell from 1% to 0.4%, the 20-year benchmark yield from 1.47% to 0.76% over the same period. 1-month, 3-month and 12-month bid rates averaged 0.61%, 0.72% and 0.88% respectively over the period.

Since the start of the calendar 2020, the yield on 2-year US treasuries had fallen from 1.573% to 0.20% and from 1.877% to 0.61% for 10-year treasuries. German bund yields remain negative.

Credit review: In Q4 2019 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 the banks' aggregate level of CET1 capital would remain twice their level before the 2008 financial crisis.

After remaining flat in January and February and between a range of 30-55bps, Credit Default Swap spreads rose sharply in March as the potential impact of the coronavirus on bank balance sheets gave cause for concern. Spreads declined in late March and through to mid-April but remain above their initial 2020 levels. NatWest Markets Plc (non-ring-fenced) remains the highest at 128bps and National Westminster Bank Plc (ring-fenced) still the lowest at 56bps. The other main UK banks are between 65bps and 123bps, with the latter being the thinly traded and volatile Santander UK CDS.

While the UK and Non-UK banks on the Arlingclose counterparty list remain in a strong and well-capitalised position, the duration advice on all these banks was cut to 35 days in mid-March.

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 the outlook on all banks on the counterparty list to negative, 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-.

Appendix C – List of Investments made and/or maturing in 2019/20

Counterparty	Principal £	From / To		Interest/Return £
Term Deposits				
Thurrock Borough Council	2,500,000	2 Oct 18	2 Apr 19	11,219.18
Thurrock Borough Council	3,000,000	14 Nov 18	14 May 19	13,389.04
Debt Management Office	4,000,000	2 Apr 19	11 Apr 19	493.15
Debt Management Office	5,000,000	1 May 19	13 May 19	821.92
Debt Management Office	3,000,000	13 May 19	22 May 19	369.86
Thurrock Borough Council	3,000,000	14 Jun 19	16 Mar 20	19,962.74
Derbyshire County Council	3,000,000	14 May 19	14 Jun 19	1,452.33
Debt Management Office	8,500,000	1 Jul 19	8 Jul 19	815.07
Debt Management Office	7,500,000	8 Jul 19	22 Jul 19	1,438.36
Debt Management Office	1,800,000	17 Jul 19	25 Jul 19	197.26
Debt Management Office	5,800,000	22 Jul 19	1 Aug 19	794.52
Debt Management Office	7,000,000	1 Aug 19	5 Aug 19	383.56
Debt Management Office	1,000,000	1 Aug 19	9 Aug 19	109.59
Debt Management Office	5,000,000	1 Aug 19	19 Aug 19	1,232.88
Debt Management Office	5,000,000	19 Aug 19	11 Sep 19	1,575.34
Debt Management Office	3,000,000	13 Sep 19	18 Sep 19	205.48
Debt Management Office	5,000,000	5 Jun 19	28 Jun 19	1,606.85
Debt Management Office	6,000,000	1 Oct 19	17 Oct 19	1,328.22
Stockport Metropolitan Borough Council	5,000,000	3 Dec 19	3 Feb 20	5,775.34
Cheltenham Borough Council	3,000,000	12 Dec 19	12 Feb 20	3,567.12
Thurrock Borough Council	6,000,000	23 Jan 20	24 Feb 20	3,945.21
Thurrock Borough Council	3,000,000	25 Feb 20	25 Mar 20	2,264.38
West Berkshire Council	3,000,000	25 Feb 20	10 Mar 20	1,150.68

Glossary of Terms

Affordable Borrowing Limit	Each local authority is required by statute to determine and keep under review how much money it can afford to borrow. The Prudential Code (see below) sets out how affordability is to be measured.
Base Rate	The main interest rate in the economy set by the Bank Of England, upon which others rates are based.
Bonds	Debt instruments issued by government, multinational companies, banks and multilateral development banks. Interest is paid by the issuer to the bond holder at regular pre-agreed periods. The repayment date of the principal is also set at the outset.
Capital Expenditure	Spending on the purchase, major repair, or improvement of assets e.g. buildings and vehicles.
Capital Financing Requirement (CFR)	Calculated in accordance with government regulations, the CFR represents the amount of Capital Expenditure that it has incurred over the years and which has not yet been funded from capital receipts, grants or other forms of income. It represents the Council's underlying need to borrow.
Chartered Institute of Public Finance and Accountancy (CIPFA)	CIPFA is one of the leading professional accountancy bodies in the UK and the only one that specialises in the public services. It is responsible for the education and training of professional accountants and for their regulation through the setting and monitoring of professional standards. Uniquely among the professional accountancy bodies in the UK, CIPFA has responsibility for setting accounting standards for a significant part of the economy, namely local government.
Counterparty	Organisation with which the Council makes an investment.
Credit Default Swaps	CDS are a financial instrument for swapping the risk of debt default and are effectively an insurance premium. Local authorities do not trade in CDS but trends in CDS prices can be monitored as an indicator of relative confidence about the credit risk of counterparties.
Credit Rating	A credit rating is an independent assessment of the credit quality of an institution made by an organisation known as a rating agency. The rating agencies take many factors into consideration when forming their view of the likelihood that an institution will default on their obligations, including the institution's willingness and ability to repay. The ratings awarded typically cover the short term outlook, the long term outlook, as well as an assessment of the extent to which the parent company or the state will honour any obligations. At present the three main agencies providing credit rating services are Fitch Ratings, Moody's and Standard and Poor's
Fixed Deposits	Loans to institutions which are for a fixed period at a fixed rate of interest.
Gilts	These are issued by the UK government in order to finance public expenditure. Gilts are generally issued for set periods and pay a fixed rate of interest. During the life of the gilt it will be traded at price decided in the market.

Housing Revenue Account (HRA)	There is a statutory requirement for local authorities to account separately for expenditure incurred and income received in respect of the dwellings that they own and manage.
Lenders' Option Borrower's Option (LOBO)	A long term loan with a fixed interest rate. On pre- determined dates (e.g. every five years) the lender can propose or impose a new fixed rate for the remaining term of the loan and the borrower has the 'option' to either accept the new imposed fixed rate or repay the loan.
LIBID	The rate of interest at which first-class banks in London will bid for deposit funds.
Minimum Revenue Provision (MRP)	The minimum amount which must be charged to an authority's revenue account each year and set aside as provision for the repayment of debt.
Operational boundary	This is the most likely, prudent view of the level of gross external indebtedness. A temporary breach of the operational boundary is not significant.
Prudential Code/Prudential Indicators	The level of capital expenditure by local authorities is not rationed by central government. Instead the level is set by local authorities, providing it is within the limits of affordability and prudence they set themselves. The Prudential Code sets out the indicators to be used and the factors to be taken into account when setting these limits.
Public Works Loan Board (PWLB)	A central government agency which provides long-term and medium-term loans to local authorities at interest rates only slightly higher than those at which the Government itself can borrow.
Treasury Management Strategy Statement (TMSS)	Approved each year, this document sets out the strategy that the Council will follow in respect of investments and financing both in the forthcoming financial year and the following two years.
Treasury Bills (T-Bills)	These are issued by the UK Government as part of the Debt Management Office's cash management operations. They do not pay interest but are issued at a discount and are redeemed at par. T-Bills have up to 12 months maturity when first issued.