Finance Committee

Date: **5 July 2017**

Item: **Treasury Activities**

This paper will be considered in public

1 Summary

1.1 This paper provides a brief update on key Treasury activities for the period from 1 April to 16 June 2017 (the Reporting Period), as requested by the Committee. A more comprehensive update on Treasury activities is planned in Autumn 2017.

1.2 During the Reporting Period we have complied at all times with the Treasury Management Policy Statement and Treasury Management Practices and the Treasury Management Strategy approved by the Board on 29 March 2017, including the GLA Responsible Investment policy.

1.3 A paper is included on Part 2 of the agenda, which contains exempt supplemental information and documentation. The information is exempt by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972 in that it contains information relating to the financial affairs of TfL or of a sensitive nature to our listed counterparties. Any discussion of that exempt information must take place after the press and public have been excluded from this meeting.

2 Recommendation

2.1 **The Committee is asked to note the paper.**

3 Treasury Highlights

3.1 There are a number of activities undertaken by the Treasury function (now part of the Corporate Finance team) since 1 April 2017 that are of note:

(a) a £250m 10-year loan with Export Development Canada (EDC) was signed on 17 May 2017;

(b) the continued active investment management of TfL's cash portfolio, £2.4bn including Crossrail as of 16 June 2017, resulted in a year-to-date weighted average return of 0.27 per cent versus the average benchmark seven-day London Interbank Bid Rate (LIBID) of 0.11 per cent;

(c) on 18 May 2017 £150m was drawn down under the £500m EDC Crossrail Rolling Stock and Depot loan. Further drawdowns from EDC and the European Investment Bank (EIB), for a total of £800m, will take place by 31 March 2018;

(d) Treasury has actively supported the wider TfL organisation in identifying and managing financial risks (foreign exchange risk, interest rate risk, counterparties' credit risk); and

(e) Treasury has actively managed relations with external financial investors, lenders and credit rating agencies.

4 Borrowing Update

Authorised Borrowing Limit

4.1 The authorised borrowing limit for 2017/18 is £11.9bn, a number higher that the £10.4bn target debt (see paragraph 4.3) as it includes, for example, the option to raise all incremental borrowing and refinance the existing debt due to mature in year before the outstanding debt is repaid.

New EDC loan facility

4.2 On 17 May 2017, TfL signed a new £250m 10-year corporate loan facility with EDC to support the delivery of the new signalling system by Thales, as part of the Four Lines Modernisation project. The new facility represents TfL's second transaction with EDC following a £500m loan agreement signed in 2015, which supports the purchase of Crossrail rolling stock. The facility will allow TfL to forward fix interest rates and drawdown the proceeds over a period of three years.

Borrowing requirement

4.3 The table below sets out TfL's borrowing requirement as per the TfL Budget 2017/18 (TfL Budget). The TfL Budget assumes that £331m of the £950m available for borrowing (£900m incremental borrowing limit agreed with HM Treasury plus £50m of borrowing deferred from 2016/17) will be deferred to 2018/19. As at 16 June 2017, TfL had £9,978m of debt outstanding, of which £763.5m was short-term commercial paper. The weighted average interest rate on TfL's debt was 3.55 per cent (with a weighted average life of 19.3 years). The target debt for 2017/18 is £10.4bn.

Table 1: Borrowing Requirement for 2017/18

	£m
Incremental Borrowing as per Budget 2017/18 (including amount deferred from 2016/17)	619.5
Refinancing of £300m 1.250% Notes due November 2017	300
Refinancing of other debt maturing within 12 months	331
Total borrowing requirement	**1,250.5**
Financed by:	
EIB Crossrail Rolling Stock and Depot Loan (undrawn)	500
EIB Urban Mobility for London Loan (undrawn)	300
EDC Crossrail Rolling Stock and Depot Loan (drawn)	150
Total committed for 2017/18	**950**
Balance to raise for 2017/18	**300.5**

TfL's Credit Ratings

4.4 While TfL does not have any direct financial covenants, TfL does have an implicit financial covenant through its commitment to maintain its high credit rating.

4.5 Table 2 sets out TfL's current credit ratings. There have been no changes to TfL's credit ratings since June / July 2016.

Table 2: Current Credit Ratings

	Standard & Poor's	Moody's	Fitch
Long-term rating	AA	Aa2	AA-
Outlook	Negative	Negative	Negative
Short-term rating	A-1+	P-1	F1+

4.6 On 31 March 2017, Standard & Poor's Rating Services published an update on TfL's credit rating factors and affirmed our credit rating of AA with negative outlook. The report highlights our exceptional access to liquidity, along with the strategic importance and high demand for our services, but recognises challenges from ongoing grant cuts, falling cash balances and the current cost reduction programme.

4.7 The rating agencies indicated that a further downgrade of the UK Sovereign, substantially higher debt, and reduced support from the UK Government (in the form of grants reduction) are the main factors that could lead to a further TfL rating downgrade. The rating could be upgraded if the UK Sovereign is upgraded, TfL's total revenue rises to such an extent that any deficit after capital expenditure is eliminated, or if the level of debt is significantly reduced.

5 Risk Management Update

Foreign Exchange Risk

5.1 Treasury has supported commercial teams on procurements which contain foreign currency exposure for TfL. Foreign currency exposure relating to the Central Line AC Traction upgrade project has been hedged in the Reporting Period. Additional information is provided in the paper on Part 2 of the agenda.

Interest Rate Risk

5.2 As indicated in Table 1, £950m out of a total £1,250.5m budgeted borrowing requirement for 2017/18 has been pre-arranged at fixed rates of interest, leaving only £300.5m exposed to interest rate fluctuations once the associated interest rate swaps mature. Given current interest rate expectations, TfL considers its exposure to interest rate risk relative to the 2017/18 budget to be acceptable.

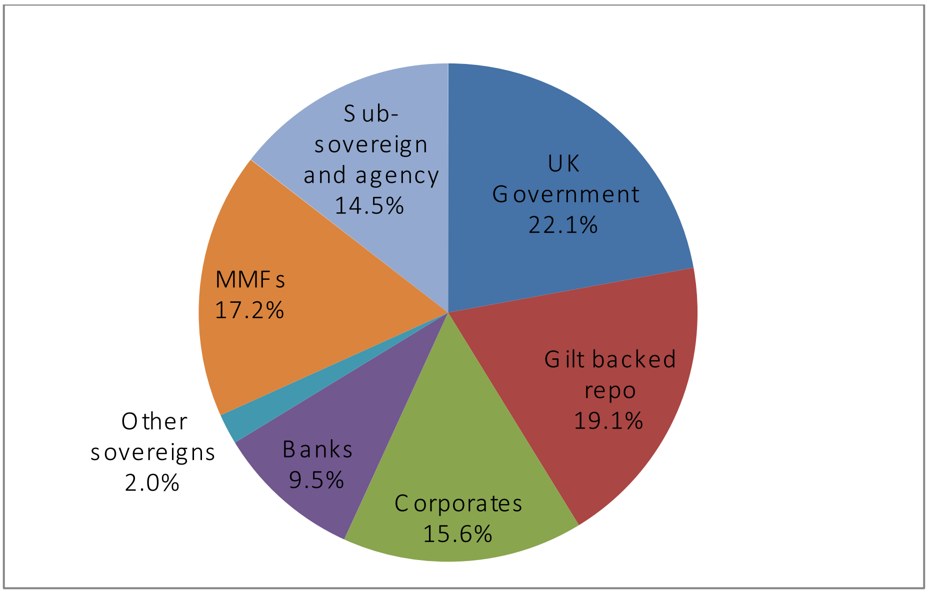
6 Investments

6.1 TfL has complied with Board approved investment limits and the GLA policy for Responsible Investment at all times during the year to date. As part of its standard investment procedures, TfL has also implemented internal forward looking and dynamic investment limits within the Board approved counterparty investment limits. These limits allow TfL to further increase the security of cash under management.

6.2 As at 16 June 2017, TfL had £2.4bn of cash under management, including £0.94bn of cash ring-fenced to fund the construction of the Crossrail project.

6.3 TfL’s cash balances have been built up as a result of securing the most favourable funding and financing terms for TfL’s capital investment programme to a pre-agreed schedule with Government which sometimes comes in advance of delivery of major projects – including for example Crossrail. All of the cash under management above the target minimum cash level is allocated to planned projects within the Business Plan. The allocation of TfL’s cash investments is summarised in Chart 1 below.

Chart 1: Cash Investment Allocations as of 16 June 2017



6.4 TfL’s year-to-date average yield at 16 June 2017 was 0.27 per cent, 16 basis points above the seven day LIBID benchmark, which is widely regarded as the market benchmark for short term cash investments for professional investors, such as Money Market Funds (MMFs).

6.5 Active management of the investment portfolio by Treasury has resulted in a greater return compared to a passive approach that would involve investing cash surpluses in MMFs only. This higher rate of return is being achieved while holding much higher credit quality investments than those held by the MMFs. TfL has continued to benefit from a favourable return versus risk profile, mostly from having the ability to invest in both Euro and Dollar denominated corporate paper and swapping back to Sterling.

7 Other Activities

Banking

7.1 Changes in banking regulations pursuant to the Financial Services (Banking Reform) Act 2013 mean that TfL's banking provider must ring-fence its UK retail banking operations from any wholesale or investment banking activity. Therefore all TfL bank accounts will need to migrate to a new sort code and account number. A full impact assessment has been completed and a project team is in place actively managing milestones to ensure delivery by the go live date of 1 October 2017.

7.2 The EU Capital Requirements Directive IV and the Capital Requirements Regulation575/ 2013 imposed new requirements on the way banks have to report notional pooling to central banks, which necessitated changes to legal documentation related to pooling arrangements.

List of appendices to this report:

Exempt supplementary information is included in a paper on Part 2 of the agenda.

List of Background Papers:

None

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