CABINET

Agenda Item: 13

Ward: **All**

Portfolio: **All**

FROM: **Corporate Finance** **Date: 5 December 2016**

SUBJECT: **Treasury Management Annual Report 2015/16**

Report Sign off	**Seen by:**	**Name**	**Date**
	Chief Executive/ Deputy Chief Executive(s)	Stuart Brown	15 November 2016
	Legal	N/A	
	Finance	Duncan Moss	15 November 2016
	Group Manager	Paul Deal	15 November 2016
	Portfolio Holder	Cllr Parham	15 November 2016
	Ward Member(s)	ALL	
Summary:	The Treasury Management Annual Report reflects on the performance against the Treasury Management strategy for the 2015/16 financial year.		
Recommendation:	**Cabinet are asked to note the report.**		
Direct and/or indirect impact on service delivery to our customers and communities	None as a direct result of this report.		
Contribution to Corporate Priorities:	The strategy has the potential to directly impact on all delivery of the corporate priorities through the capital programme		
Legal Implications:	None as a direct result of this report.		
Financial Implications:	The Strategy will impact on the financing of the Capital programme and the interest income achievable will be reflected in the revenue budgets. The aim is for the best financial return for the minimum exposure to risk.		
Impact on Service Plans:	The strategy has the potential to indirectly impact on all service plans through the capital programme		
Crime and Disorder Implications:	None as a direct result of this report.		
Equalities Implications:	None as a direct result of this report.		
Risk Assessment and Adverse Impact on Corporate Actions:	Treasury Management performance is influenced by global and national economic conditions. Restrictions set out in the manager's contract limit the institutions in which investments can be made, limit the Fund's exposure to the gilts market and control market risk.		

INTRODUCTION

The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2015/16. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

During 2015/16 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 23/02/2015)
- a mid-year (minimum) treasury update report (Council 09/11/2015)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Scrutiny Committee before they were reported to the full Council.

THE ECONOMY AND INTEREST RATES

Market expectations for the first increase in Bank Rate moved considerably during 2015/16, starting at quarter 3 2015 but soon moving back to quarter 1 2016. However, by the end of the year, market expectations had moved back radically to quarter 2 2018 due to many fears including concerns that China's economic growth could be heading towards a hard landing; the potential destabilisation of some emerging market countries particularly exposed to the Chinese economic slowdown; and the continuation of the collapse in oil prices during 2015 together with continuing Eurozone growth uncertainties.

These concerns have caused sharp market volatility in equity prices during the year with corresponding impacts on bond prices and bond yields due to safe haven flows. Bank Rate, therefore, remained unchanged at 0.5% for the seventh successive year. Economic growth (GDP) in 2015/16 has been disappointing with growth falling steadily from an annual rate of 2.9% in quarter 1 2015 to 2.1% in quarter 4.

The sharp volatility in equity markets during the year was reflected in sharp volatility in bond yields. However, the overall dominant trend in bond yields since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have repeatedly been revised downwards and expectations of increases in central rates have been pushed back. In addition, a notable trend in the year was that several central banks introduced negative interest rates as a measure to stimulate the creation of credit and hence economic growth.

The ECB commenced a full blown quantitative easing programme of purchases of Eurozone government and other bonds starting in March at €60bn per month. This put downward pressure on Eurozone bond yields. There was a further increase in this programme of QE in December 2015.

As for America, the economy has continued to grow healthily on the back of resilient consumer demand. The first increase in the central rate occurred in December 2015 since when there has been a return to caution as to the speed of further increases due to concerns around the risks to world growth.

The UK elected a majority Conservative Government in May 2015, removing one potential concern but introducing another due to the promise of a referendum on the UK remaining part of the EU. The government maintained its tight fiscal policy stance but the more recent downturn in expectations for economic growth has made it more difficult to return the public sector net borrowing to a balanced annual position within the period of this parliament.

OVERALL TREASURY POSITION AS AT 31 MARCH 2016

At the beginning and the end of 2015/16 the Council's treasury position was as follows:

(Taken from the Statement of Accounts 2015/16)	**31ST March 2015 £000**	**31st March 2016 £000**
Short-term Borrowing	(20)	(20)
Long-term Borrowing	(182)	(162)
Short-term Investments	1,656	7,636
Long-term Investments	0	0
Cash & Cash Equivalents	7,193	2,340

Further details of the treasury management indicators for 2015/16 can be found in Appendix 1 at the end of this report.

THE STRATEGY FOR 2015/16

The expectation for interest rates within the treasury management strategy for 2015/16 anticipated low but rising Bank Rate, (starting in quarter 1 of 2016), and gradual rises in medium and longer term fixed borrowing rates during 2016/17. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

In this scenario, the treasury strategy was to postpone borrowing to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

THE BORROWING REQUIREMENT AND DEBT

At the start of the year the Council had a small amount (£182,000) of long-term borrowing outstanding, related to residual loans undertaken before 24 August 1985. The strategy in relation to short-term borrowing of obtaining funding to meet cash flow shortages using the services of Money Market Brokers did not need to be implemented.

During the year the Council operated within the treasury limits set out in the Treasury Management Strategy and these can be seen in Appendix 1 to this report.

A Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's debt position. The CFR results from the capital activity of the Council and what resources have been used to pay for the capital spend. It represents the 2015/16 unfinanced capital expenditure (see Appendix 1), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Reducing the CFR – the Council's underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision – MRP, to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

The total CFR can also be reduced by:

(a) the application of additional capital financing resources (such as unapplied capital receipts); or

(b) charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

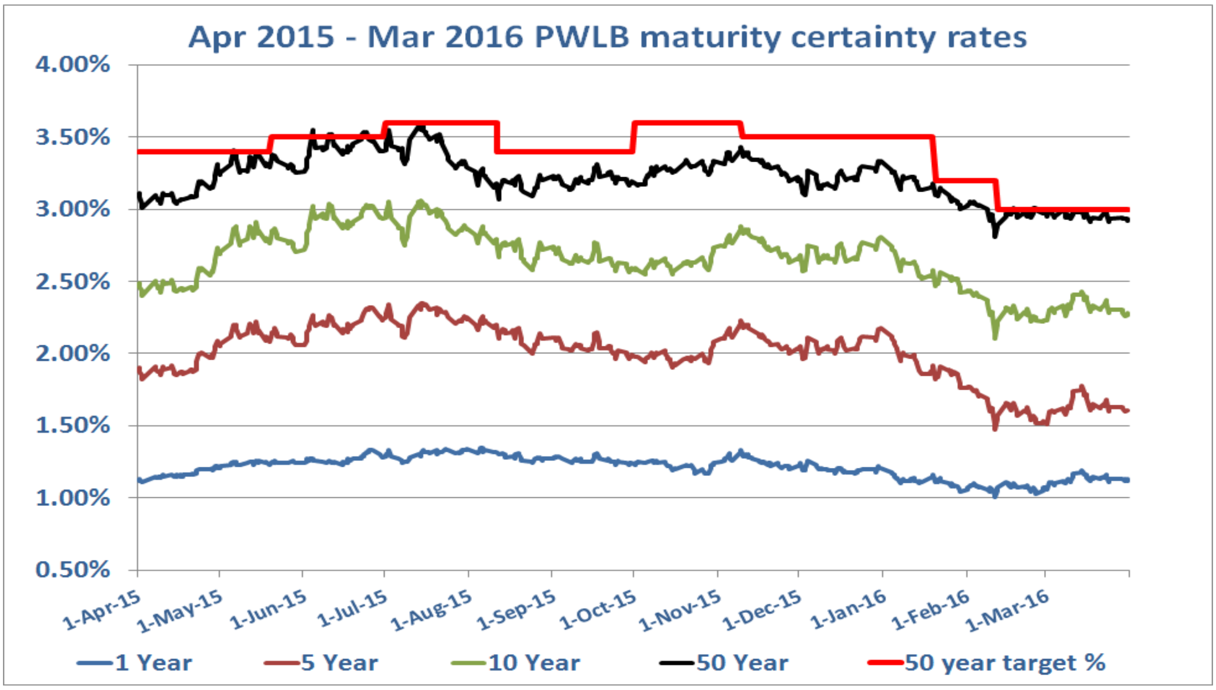
The Council has adopted the asset life method of calculating MRP where the charge is spread in equal annual instalments over the life of each asset that creates a borrowing requirement. MRP commences in the financial year following either the year in which the expenditure was incurred or the year when the asset becomes operational.

The Council's CFR for the year is shown in Appendix 1 at the end of this report and represents a key prudential indicator. This includes PFI and leasing schemes on the balance sheet, which increase the Council's borrowing need, the CFR. No borrowing is actually required against these schemes as a borrowing facility is included in the contract (if applicable).

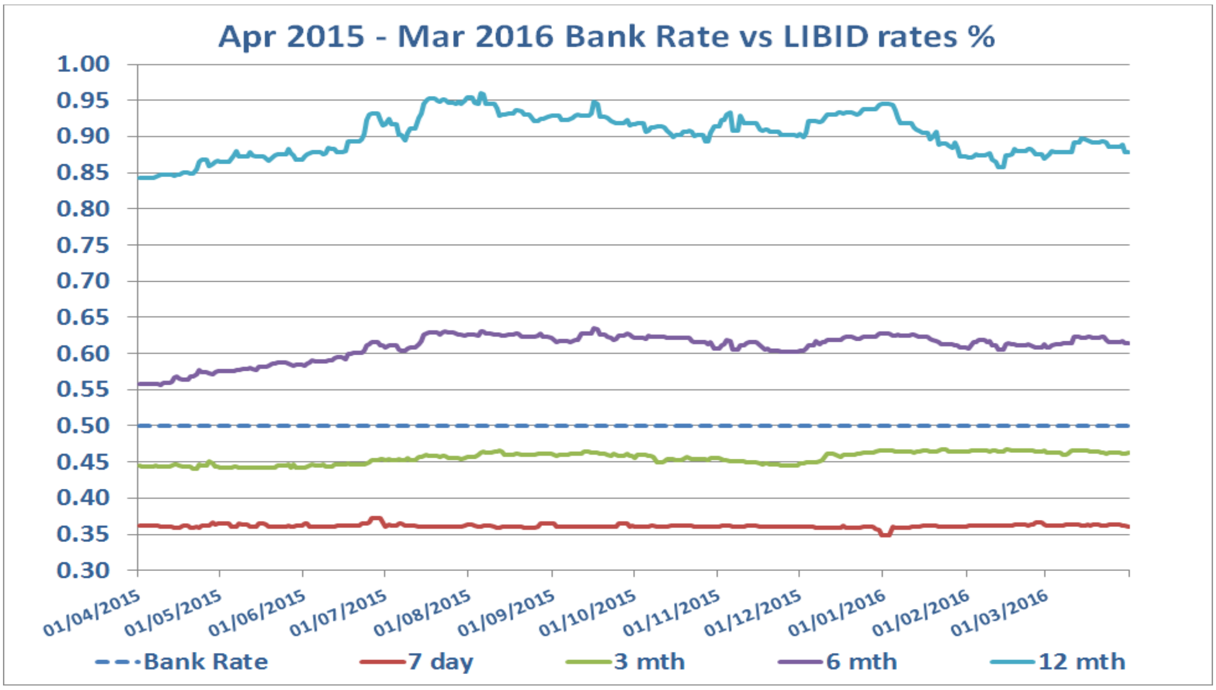
The borrowing activity is constrained by prudential indicators for net borrowing and the CFR, and by the authorised limit.

BORROWING RATES

PWLB certainty maturity borrowing rates - the graph below shows how PWLB certainty rates have fallen to historically very low levels during the year.



INVESTMENT RATES 2015/16



Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for seven years. Deposit rates remained depressed during the whole of the year, primarily due to the effects of the Funding for Lending Scheme and due to the continuing weak expectations as to when Bank Rate would start rising.

INVESTMENT OUTTURN FOR 2015/16

Investment Policy – the Council's investment policy is governed by CLG guidance, which has been implemented in the annual investment strategy approved by the Council on 23rd February 2015. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Investments held by the Council - at the end of the financial year the Council held £7,610,000 of internally managed funds and it had placed a cumulative figure of £23,613,823 million of individual investments during the year (Appendix 2). These investments earned a total interest of £71,136.50 during the year, an average rate of return of 0.71%.

The Council also held 3 call accounts, the main one at NatWest plus two others with the Bank of Scotland and Santander Bank. These accounts held varying overnight balances but did not exceed the £5 million daily limit.

Bank	Year End Balance	Interest Rate	Total Interest
Natwest	£361,050	0.25%	£6,223
Bank of Scotland	£719,371	0.40%	£14,211
Santander	£1,101,053	0.40%	£11,205

COMPLIANCE WITH TREASURY MANAGEMENT

During the financial year the Council operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Policy Statement and annual Treasury Strategy Statement. The outturn for the Prudential Indicators is shown in Appendix 1.

PROPOSAL FOR ACTION

Members are asked to note that officers have complied with the Council's Treasury Management policies and practices during the 2015/16 financial year.

RELATIONSHIP TO CORPORATE OBJECTIVES

Better Resource Management

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Background Papers (available upon request)

- 2015/16 Annual Treasury Strategy in advance of the year (Council 23/02/2015)
- 2015/16 Mid-year Treasury Update Report (Council 09/11/2015)

APPENDIX 1: PRUDENTIAL AND TREASURY INDICATORS

1. Prudential Indicators (Extract from budget setting report)	2014/15 Actual £000	2015/16 Estimate £000	2015/16 Actual £000
Capital Expenditure	**3,622**	**1,303**	**1,063**
Ratio of financing costs to net revenue stream	**0.38%**	**0.90%**	**1.18%**
Net debt (short and long term)	**202**	**182**	**182**
Capital Financing Requirement*	**3,201**	**2,432**	**2,152**
Annual change in Capital Financing Requirement	**1,947**	**172**	**-376**
Incremental impact of capital investment decisions	**%**	**%**	**%**
Increase in council tax (band D) per annum	**-1.40**	**-7.69**	**-7.72**

2. Treasury Management Indicators	2014/15 Actual £000	2015/16 Original £000m	2015/16 Actual £000m
Authorised limit for external debt			
Borrowing	10	10	10
Other long-term liabilities	0	0	0
Total	**10**	**10**	**10**
Operational boundary for external debt			
Borrowing	10	10	10
Other long-term liabilities	0	0	0
Total	**10**	**10**	**10**
Actual external debt – See Net Debt at 1 above			

The authorised limit - the authorised limit is the “affordable borrowing limit” required by Section 3 of the Local Government Act 2003. The Council does not have the power to borrow above this level. The table below demonstrates that during 2015/16 the Council has maintained gross borrowing within its authorised limit.

The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

Actual financing costs as a proportion of net revenue stream - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

APPENDIX 2: SCHEDULE OF ALL INVESTMENTS PLACED 2015/16

Borrower	Date lent	Date Repaid	Interest Rate (%)	Amount (£)	Total Interest to 31/03/2016 (£)
Lloyds Bank	19-May-15	19-Nov-15	0.70	2,000,000.00	7,057.53
Lloyds Bank	01-Jun-15	14-Dec-15	0.70	3,000,000.00	11,276.71
Nationwide	01-Jul-15	18-Jan-16	0.68	3,500,000.00	13,106.30
Standard Chartered	19-Aug-15	19-Feb-16	0.72	1,002,561.66	3,638.89
UK Government Gilt	28-Jul-15	22-Jul-18	1.25	1,610,000.00	13,618.84
Lloyds Bank	01-Dec-15	01-Sep-16	0.85	2,000,000.00	5,635.62
Sumitomo Mitsui Banking Corp.	01-Dec-15	16-Mar-16	0.56	3,000,260.95	4,879.33
Bank of Scotland	02-Dec-15	02-Jun-16	0.75	3,000,000.00	7,397.26
Nationwide	09-Dec-15	22-Feb-16	0.44	1,500,000.00	1,356.16
Barclays	13-Jan-16	18-Mar-16	0.47	2,000,000.00	1,673.97
Barclays	13-Jan-16	13-Jul-16	0.70	1,000,000.00	1,495.89
				23,612,822.61	**71,136.50**