Meeting: Council **Date: 24 September 2016**

Wards Affected: All Wards in Torbay

Report Title: Treasury Management Outturn 2014/2015

Is the decision a key decision? No

When does the decision need to be implemented?

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1. Proposal and Introduction

1.1 This report informs Members of the performance of the Treasury Management function in supporting the provision of Council services in 2014/15 through management of cash flow, debt and investment operations and the effective control of the associated risks.

1.2 The headline points of the report are:

- No new borrowing during the year to fund the Capital Investment Plan
- Capital expenditure of £4.5million funded from existing borrowing
- Annual investment rate achieved exceeded the market benchmark
- Treasury Management activities achieved a saving of £300,000 on the approved budget target

2. Reason for Proposal

2.1 The Council is required through regulations issued under the Local Government Act 2003 to produce an annual outturn report reviewing treasury management activities and the actual prudential and treasury indicators for 2014/15.

2.2 This report also meets the requirements of the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

3. Recommendations

3.1 That the Treasury Management decisions made during 2014/15, as detailed in the submitted report be noted; and

3.2 That the Prudential and Treasury Indicators as set out in Appendix 1 to the submitted report be approved.

4 Background Information

4.1 Treasury management is defined by the Code of practice as:

"The management of the authority's investments and cash flows, it's 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".

4.2 During 2014/15 the minimum reporting requirements were that full Council should receive the following reports:

- An annual treasury strategy in advance of the year (Council 6th February 2014)
- A mid-year review report (distributed to all Members on the Council's intranet site in December 2014)
- An annual report following the year describing the activity compared to the strategy (this report)

4.3 The current regulatory environment places a much greater onus on Members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the policies previously approved by Members.

4.4 The Council also 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 Audit Committee before they were reported to full Council.

4.5 A major element of the Treasury Management function is the implementation and control of the Council's borrowing decisions. Like all local authorities Torbay Council uses borrowing as a key source of funding for enhancing, purchasing or building assets within the approved capital plan.

4.6 Borrowing allows the repayment costs of capital expenditure to be spread over future years which means that the costs of roads, schools etc are more likely to be met by those who use the assets than would be the case if the full cost of providing these facilities were met by taxpayers at the time of their construction.

4.7 As part of the annual budget process the Council sets limits for the total amount of borrowing that it considers is affordable in terms of revenue resources available to make repayments. Treasury Management officers are tasked with maintaining borrowing within these levels and obtaining best value for the Council in terms of repayment rates and length of loans.

4.8 The Treasury Management team also carry out management of the Council's surplus cash balances arising from, for example:

- Short term revenue balances (working capital)
- Cash backed reserves

- Capital funding received in advance of commencement of schemes

Balances are invested with approved financial institutions and other local authorities to obtain the best return for periods which ensure cash is available when needed. Security of cash and liquidity are the absolute priorities in all investment decisions.

4.9 Treasury Management strategies were planned and implemented in conjunction with the Council's appointed advisors, Capita Asset Services although the Council officers were the final arbiters of the recommended approach.

4.10 This report covers:

- The Strategy for 2014/15;
- Treasury Position at year End;
- The Economy and Interest rates 2014/15;
- Borrowing Rates in 2014/15;
- Borrowing Outturn for 2014/15;
- Investment Rates in 2014/15;
- Investment Outturn for 2014/15;
- Revenue Budget Performance;
- Reporting Arrangements and Management Evaluation

5 The Strategy for 2014/15

5.1 The central strategy for the medium term aimed to reduce the level of borrowing levels by a target of £10million over four years to reduce the credit risk and cost incurred by holding high levels of investment.

5.2 The strategy acknowledged however that interest rate outlook anticipated very little opportunity to reduce borrowing during 2014/15 due to high repayment costs. The expectation for interest rates anticipated flat levels through most of the year with minimal rises at the back end, still well below the threshold for economic borrowing repayment.

5.3 Investment strategy was strongly influenced by market and credit risk considerations and centred on secure longer term deposits (ie: one to two years), balanced by a proportion of funds maintained in business reserve and notice accounts to ensure appropriate liquidity was maintained.

6 Treasury Position at Year End

6.1 The Council's funding and investment positions at the beginning and end of year was as follows:

	31 March 2014 Principal		Rate/ Return	Average Life yrs	31 March 2015 Principal		Rate/ Return	Average Life yrs
Variable Rate Funding:		£0.0m				£0.0m		
Fixed rate funding:								
-PWLB[1]	£128.1m				£128.1m			
-Market	<u>£10.0m</u>	£138.1m	4.39%	25.0	<u>£10.0m</u>	£138.1m	4.39%	24.0
Total Borrowing		*£138.1m*	*4.39%*	*25.0*		*£138.1m*	*4.39%*	*24.0*
Other Long Term Liabilities		£8.8m	5.26%	13.5		£8.4m	5.26%	12.5
Total Borrowing/Other LTL		***£146.9M***	***4.44%***	***24.3***		***£146.5M***	***4.44%***	***23.3***
CFR[2]		***£135.1m***				***£135.3m***		
Borrowing in excess of CFR		***£11.8m***				***£11.2m***		
Approved borrowing in Capital Investment Plan		***£25m***				***£21m***		
Investments:								
- in house		£42.2m	1.25%			£39.7m	0.88%	
- with managers[4]		£29.8m	0.82%			£30.0m	0.88%	
Total investments		***£72.0m***	***1.11%***			***£69.7m***	***0.88%***	

[1]PWLB = The Public Works Loan Board,a government agency responsible for lending to Local Authorities and the Council's prime source of borrowing

[2] The Capital Financing Requirement (CFR) represents the Council's underlying need to borrow to fund capital expenditure.

[3] Rates for investments reflect the average rate achieved over the full year.

[4] The principal for external management of funds reflects the original amount applied to the contract in 2007 and subsequent additions and withdrawals

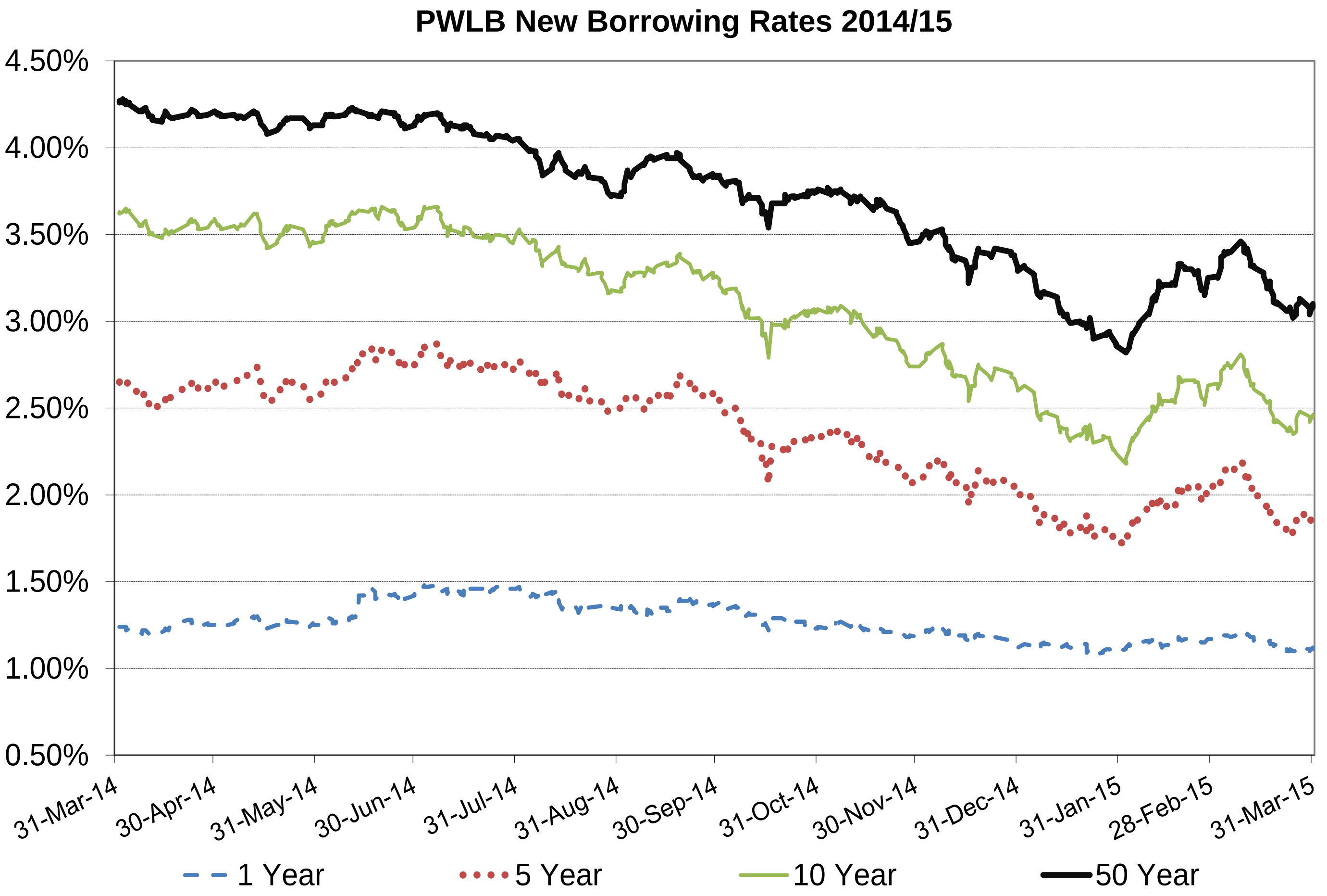
6.2 The Council is required by the specific codes of practice to measure the outturn performance against approved treasury and prudential indicators and this is detailed at Appendix 1 to this report.

7 The Economy and Interest Rates 2014/15

7.1 A commentary of the economic factors prevalent in 2014/15 is given at Appendix 2.

8 Borrowing Rates in 2014/15

8.1 The graph below illustrates the fall of PWLB new borrowing rates to historically very low levels during the year, before rising on the announcement of quantitative easing by the European Central Bank. Repayment rates are around 1% lower on those illustrated.



9 Borrowing Outturn for 2014/15

9.1 As anticipated, the falling path in borrowing rates did not allow any opportunity to early repay any of the Council's PWLB loans.

9.2 A dialogue was opened with Barclays to discuss a potential for repayment of the market loan with the bank but this too was hampered by the market conditions and the repayment cost+ was significantly unaffordable

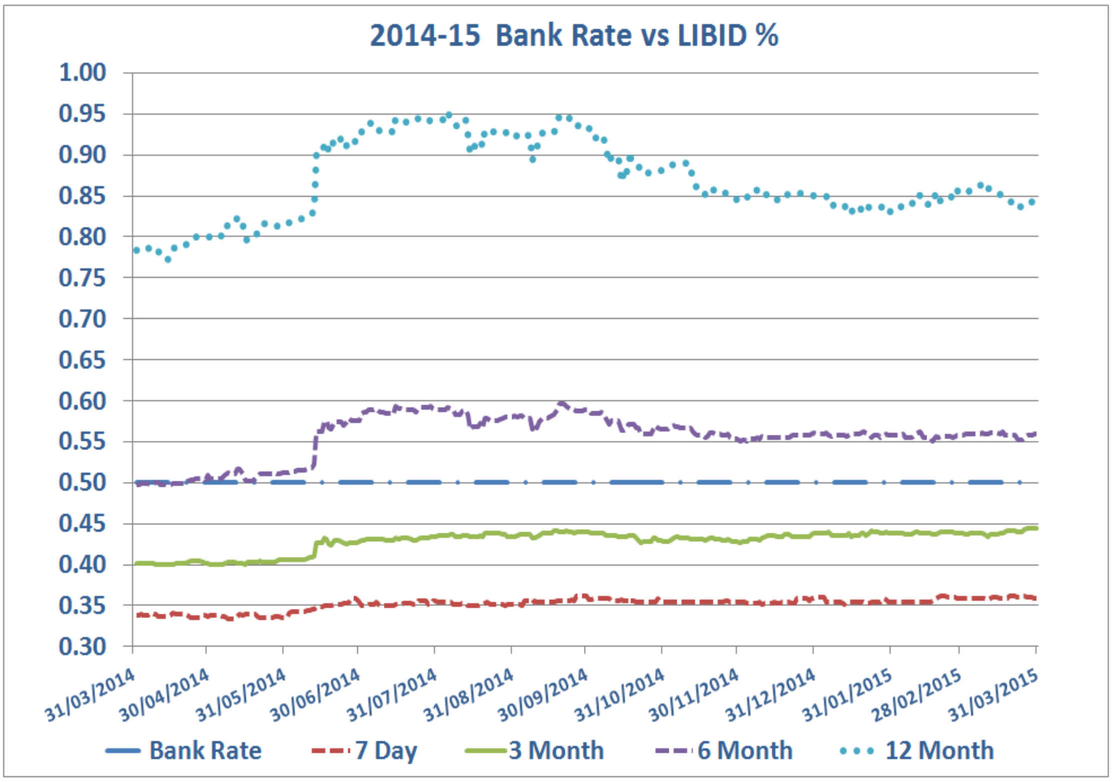
9.3 The borrowing portfolio (excluding other long term liabilities) remains at £138.1million and the average rate of interest paid on all loans in 2014/15 was 4.39% with an average maturity of 24 years.

10. Investment Rates in 2014/15

10.1 Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for six years. At the start of the year the market anticipated the rise would occur during quarter 1 2015 but was revised to around quarter 3 2016 by the end of the year.

10.2 Deposit rates remained depressed during the whole of the year, primarily due to the effects of the Funding for Lending Scheme (government supply of cheap funding to Banks to on-lend to businesses).

10.3 The following graph illustrates the path of Bank Rate against market investment rate movements during 2014/15. The affect of the changing sentiment on Bank Rate can be seen in the longer term rates (6 month/1 year) with Funding for Lending contributing to very flat levels in the short terms.
("LIBID = the representative rates which Banks will pay to each other for funding)



11. Investment Outturn for 2014/15

11.1 **Investment Policy** – the Council's investment policy is governed by CLG guidance which emphasises the priorities of security and liquidity of funds and requires Local Authorities to set out their approach for selecting suitable counterparties. The policy was approved by Council within the Annual Investment Strategy on 6th February 2014 and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data.

11.2 Due to the continuing concerns around EU sovereign debt an exclusion of Eurozone Banks from the approved counterparty list, determined by the Chief Finance Officer, remained in place throughout the year.

11.3 The limits imposed on creditworthiness gave rise to a limiting number of acceptable and practical counterparties in which to invest during the year.

11.4 In line with the approved strategy a number of one and two year deals were made with the part-nationalised banks (Lloyds Bank and Royal Bank of Scotland) locking into higher returns with a low risk of market rate increases. Remaining cash was generally deposited in lower yielding short term accounts to maintain liquidity and balance the overall risk of the investment portfolio.

11.5 Going forward, officers are conscious that the new government is likely to step up the divestment of Lloyds Bank and accordingly have recently re-classified the Bank to a higher risk level within the counterparty policy.

11.6 A list of those institutions with which the in-house team invested funds during the year is provided at Appendix 3. No institutions with which investments were made showed any difficulty in repaying investments and interest in full during the year.

11.7 ***Externally Managed Investments*** – Aberdeen Asset Management manages a proportion of the Council's investment balances to add value by way of market knowledge and exposure to a greater diversity of investments and counterparties.

11.8 ***Performance Analysis*** - Detailed below is the result of the investment strategy undertaken by the Council. Despite the continuing difficult operating environment the Council's investment returns remain well in excess of the benchmark.

	Average Investment Principal	Rate of Return (gross of fees)	Rate of Return (net of fees)	Capita Benchmarking Club		Market Benchmark/ Target Return
				Peer LA Comparison	English Unitaries	
Internally Managed	£54million	0.88%		0.77%	0.86%	0.35%
Externally Managed	£30million	0.87%	0.72%			0.35%

The benchmark for internally managed funds is the average 7-day LIBID rate (uncompounded).
The benchmark for externally managed funds is the 7-day LIBID rates, averaged for the week and compounded weekly.

11.9 In interest terms, the in-house treasury function contributed an additional £286,000 to the General Fund over and above what would have been attained from the benchmark return. Aberdeen's net return achieved an additional £87,000 over their target return level of 10% above benchmark.

12. Revenue Budget Performance

12.1 The effect of the decisions outlined in this report on the approved revenue budget is outlined in the table below.

	Revised Budget 2014/15	Actual 2014/15	Variation
	£M	**£M**	**£M**
Investment Income	(0.5)	(0.7)	(0.2)
Interest Paid on Borrowing	6.1	6.1	0.0
Net Position (Interest)	**5.6**	**5.4**	**(0.2)**
Minimum Revenue Provision (MRP)	4.3	4.2	(0.1)
MRP re: PFI	0.5	0.5	0.0
PFI Grant re: MRP	(0.5)	(0.5)	0.0
Net Position (Other)	**4.3**	**4.2**	**(0.1)**
Net Position Overall	**9.9**	**9.6**	**(0.3)**

12.2 The changing position was regularly reported to OSB and Council throughout the year as part of the budget monitoring reports to Members.

13. Reporting Arrangements and Management Evaluation

13.1 The management and evaluation arrangements identified in the annual strategy and followed for 2014/15 were as follows:

- Monthly monitoring report to Executive Lead for Finance, Chief Finance Officer and Group Leaders
- Regular meeting of the Treasury Manager and Chief Accountant to review previous months performance and plan following months activities
- Periodic meetings with the Council's treasury advisors
- Periodic meetings with the Council's appointed Fund Manager
- Membership and participation in both the CIPFA and Capita Treasury Services Benchmarking Club (the CIPFA membership has not been renewed in 2015/16)

Appendices

Appendix 1 Prudential and Treasury Indicators 2014/15
Appendix 2 The Economy and Interest Rates in 2014/15
Appendix 3 Counterparties with which funds have been deposited in 2014/15

Background Documents
Treasury Management Strategy 2014/15