Finance Sub-Committee – 6 February 2017

Treasury Management Report to 31 December 2016

Purpose of report

The purpose of this report is to note the current position for Treasury Management for the period to 31 December 2016 in financial year 2016/17.

Attachment(s)

Appendix 1: Prudential Indicators – as at 31 December 2016/17

1. Introduction

1.1. The Treasury Management Strategy for 2016/17 was approved as part of the Medium Term Financial Strategy (MTFS) in February 2016. It was underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2009.

1.2. The CIPFA Code of Practice recommends that Members be informed of treasury management activities at least twice a year; this report therefore embraces best practice.

1.3. The report provides:

- A summary of the economic conditions affecting the council's investment strategy
- Details of investments made during the year
- A summary of the council's current investment portfolio

1.4. The council's investment priorities are:

- Security of capital invested
- Liquidity of capital invested
- Return on investment

2. Market Conditions

2.1 **Growth:** Change in gross domestic product (GDP) is the main indicator of economic growth. 3rd quarter growth came in at 0.5%, some way ahead of the Bank of England and market expectations.

The European Central Bank (ECB) has left its main policy for interest rates at -0.4%, but announced changes to its bond-buying programme. The current €80bn monthly purchase is set to be reduced to €60bn from April 2017. The market expectation for the interest rate was predicted, but the reduction in monthly purchases was a surprise.

The Federal Reserve in December decided to increase interest rates and the bank suggests that there will be further interest raises in the light of further growth in 2017. However, the full extent of the new Presidents fiscal boost are yet to be realised where any upside impact on inflation may yet see more rate hikes than currently expected.

2.2 **Inflation:** The Consumer Prices Index (CPI) increases are higher than expected, though average prices fell modestly on a monthly basis in December, they are up

10% y/y, which will contribute to rises in both CPI and RPI inflation measures. CPI is forecast to rise to around 1.4%, which would be the highest since August 2014.
So far the impact of sterling weakness has not really passed through into the annual CPI rate increase seen so far, suggesting that this will filter through in 2017 as import prices increase.

2.3 **Monetary Policy:** The Monetary Policy Committee (MPC) voted unanimously in favour of maintaining the bank rate at 0.25% and re-enforcing its commitment to keep the Quantitative Easing (QE) programme at £435bn.

As the fallout from the EU Referendum vote has, for the time being, become slightly steady, evaporating any short term interest rate cut; the BoE indicated that interest rates are just as likely to go up as down.

2.4 **Interest Rates:** The latest forecast for interest rates, based on information from the council's Treasury Management advisors, is shown below:

Official Bank Rate	Q4 16	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18	Q3 18
Capita	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25

3. Treasury Management Activity

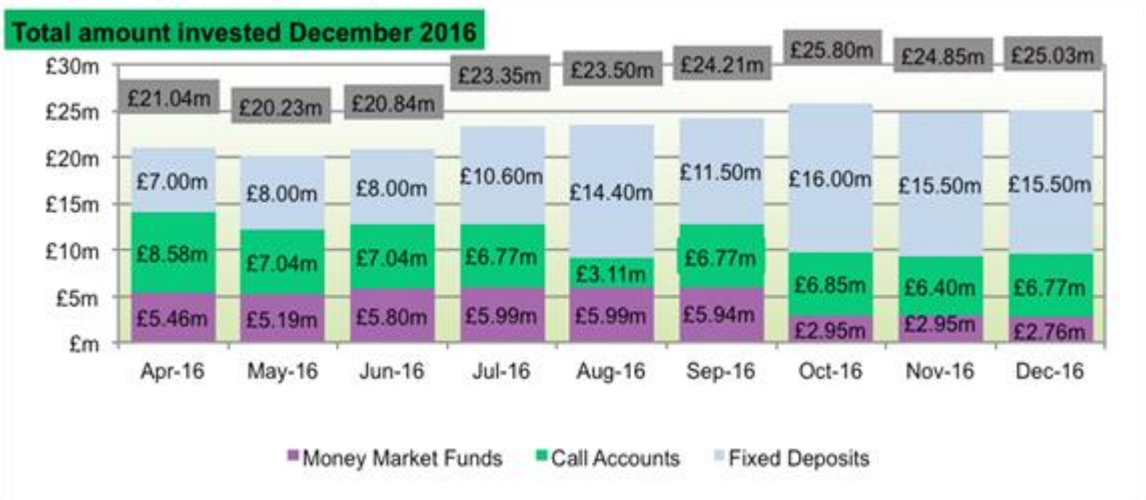
3.1. During the first four months of the 2016/17 financial year, the opportunity for the council to invest its surplus cash for periods beyond 3 to 6 months in duration has been limited. This has mainly been due to the impact of the uncertainty in the lead up to the EU Referendum vote as well as the impact following the outcome of the vote.

3.2. Investing for shorter durations reduces the counterparty risk the council is exposed to and the potential yield (interest rate) the council can achieve. However, since the impact of the EU Referendum vote and the Bank of England's decision to reduce interest rates further, any yield achievable on surplus cash balances has been and is expected to continue to be reduced. To mitigate some of the impact of reduced rates, the council opted for fixed term deposits, by investing in a 30 day notice account, which was yielding 1%, but from September onwards this was reduced to below 1%.

3.3. The council will continue to monitor the economic outlook and money markets to ensure it is able to achieve a yield in line with market expectations whilst ensuring security and liquidity of capital are maintained.

3.4. Future investment decisions are discussed between the Treasury Manager and Finance Manager and are made in line with the Annual Treasury Management Strategy approved by Council and the advice from the council's Treasury Management Advisors.

3.5. The charts below demonstrate the change in investment by type up to 31 December 2016.



3.6. Call accounts and Money Market Funds (MMF) are very short term, liquid investments. They are generally overnight deposits or short term notice accounts where the balance invested can be withdrawn immediately. Fixed Deposits are investments with a longer duration, where cash is invested for a contractually agreed period with no opportunity to withdraw cash prior to the maturity date of the deposit.

3.7. The level of cash balances held by the council has increased since April 2016 by £3.99m. An explanation is provided later in this report (see paragraph 4.4).

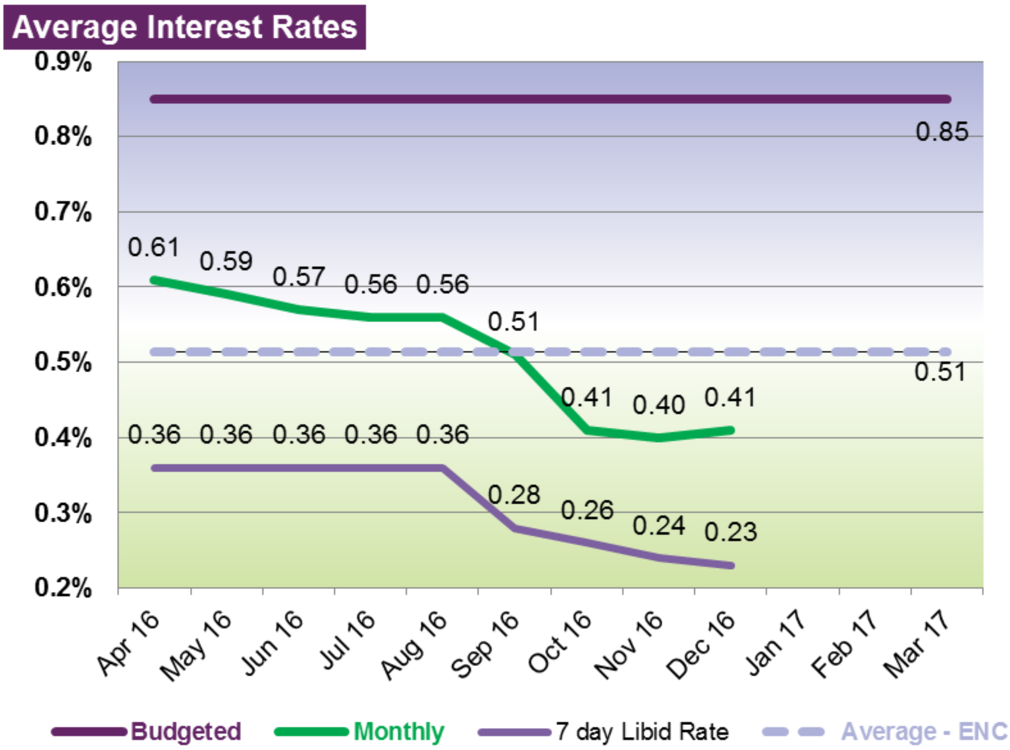
4. Treasury Management Position and Performance

4.1. The table below summarises the council's current portfolio of investments as at 31 December 2016.

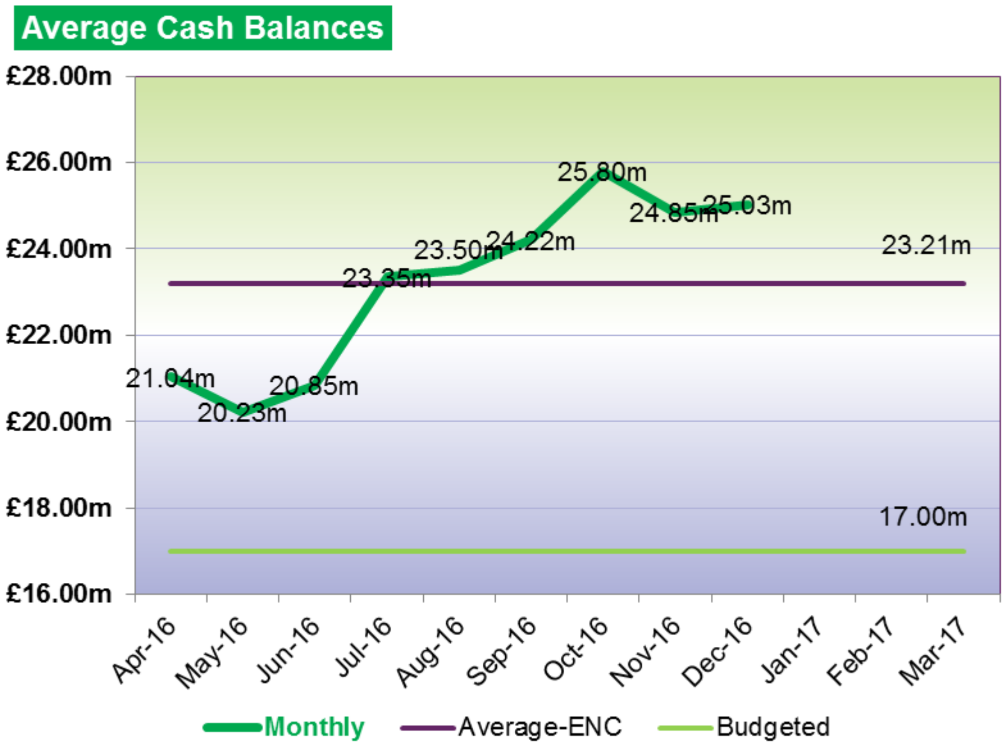
Counterparty / Lender	Amount	Rate %	Maturity Date
Call Accounts			
Santander UK (95 Day notice)	£1,500,000	0.65	
Santander UK (180 Day notice)	£1,500,000	0.90	
Barclays Bank Current Account	£786,498	0.05	
Money Market Funds			
Federated Sterling Liquidity Fund (Money Market Fund)	£2,752,583	0.31	
Fixed Term Deposits			
Close Brothers	£2,987,955	0.25	21/01/2017
Debt Management Office (Treasury)	£1,500,000	0.15	05/01/2017
Coventry Building Society	£3,000,000	0.50	11/01/2017
Lloyds Bank	£1,000,000	0.65	08/02/2017
Lloyds Bank	£2,000,000	0.65	25/04/2017
Telford & Wrekin Council	£2,500,000	0.30	28/03/2017
Blaenau Gwent County	£2,500,000	0.27	16/02/2017
Nationwide Building Society	£3,000,000	0.55	04/01/2017
	£25,027,036		

4.2. The average return on the council's portfolio to 31 December 2016 is 0.41%. This is 0.18% above the average 7-day London Interbank Bid Rate (LIBID) of 0.23%.

4.3. The council's current interest rate achievable on its investment portfolio is lower than anticipated when the budget was set in February 2016. At that time, the expected rate was 0.85%. This is demonstrated in the table below:



4.4. Whilst the council's investments are achieving lower rates of return, the level of cash balances held by the council is higher than anticipated when the budget was set in February 2016, as demonstrated in the table below. The majority of the increase in cash balances is due to the timing of Council Tax and Business Rates receipts and slippage within the Capital Expenditure Programme.



4.5. During 2015/16, the higher level of cash balances resulted in a higher amount of interest earned for the council. However, for 2016/17, due to the downturn in interest rates, the interest receivable is expected to be below budget by approximately £36.9k.

4.6. The council continues to make use of its surplus monies, meaning there has been no requirement to undertake any external borrowing. Consequently, no interest payable has been incurred during this period.

4.7. The overall Treasury Management outturn is set out below.

Treasury Management Budget vs. Estimated Outturn				
	Budget £	Estimated Outturn £	Pressure £	
Investments	£144,500	£107,610	(£36,890)	Lower interest rates being achieved, partly offset by higher than expected cash balances
Total	**£144,500**	**£107,610**	**(£36,890)**	

5. Prudential Indicators

5.1. Prudential Indicators look at the council's capital expenditure in terms of affordability and sustainability over the medium term and in particular the impact of these capital investment decisions on Council Tax. Details of each of the prudential indicators are shown in **Appendix 1.**

5.2. A key indicator for the council is the Ratio of Financing Costs to Net Revenue Stream. As the council has no external borrowing, the indicator for affordability is zero which is line with what was estimated. Further detail on this indicator can be seen in appendix 1 (paragraph 1).

5.3. Another key indicator for the council is the Incremental Impact of Capital Investment Decisions on cash surpluses. This shows the impact of the capital investment in terms of the potential increase in the Council Tax funding requirement, i.e the opportunity costs (interest receivable) of not being able to invest these surplus funds elsewhere. During 2016/17 the council has decreased its investment within the capital programme and therefore the impact on Council Tax has decreased. Additionally, the interest rate foregone is lower than budgeted at 0.41% compared to 0.85%. The reduction in interest rates has allowed the council to ensure its capital expenditure remains affordable and sustainable. Further detail can be found in Appendix 1 (paragraph 3).

	2016/17 Estimate	2016/17 Actual
Capital Expenditure	£1,773,005	£1,720,322
Increase in Band D Council Tax	0.50p	0.32p

6. Equality and Diversity Implications

6.1. This report is for information. There are no equality and diversity implications arising from the content.

7. Legal Implications

7.1. This report is for information. There are no legal implications arising from the content.

8. Risk Management

8.1. This risks arising from Treasury Management activity are recorded in the Risk Register. The risks are subject to regular review and update.

9. Resource and Financial Implications

9.1. This report is for information, there are no financial implications arising from this report.

10. Constitutional Implications

10.1. The report does not require any amendment to the Council's Constitution.

11. Customer Service Implications

11.1. There are no customer service implications arising from the report.

12. Corporate Outcomes

- ***Good Value for Money***
  This report demonstrates that the council is ensuring it effectively manages its surplus cash to achieve good value for money for the Council
- ***Effective Management***
  Treasury Management allows the council to manage its surplus cash balances to ensure the main principles (Security, Liquidity, and Yield) are maintained, contributing to effective management of the council

13. Recommendations

13.1. Finance Sub-Committee is recommended to:

a) note the Treasury Management performance for period 9 of 2016/17;

(Reason – in accordance with CIPFA guidance and best practice in Treasury Management)

Legal	Power: Local Government Finance Act 2002 Other considerations:				
Background Papers:					
Person Originating Report:	Michelle Drewery, Finance Manager, 01832 742267 mdrewery@east-northamptonshire.gov.uk				
Date: 22/01/2017					
CFO		**MO**		**CX**	

Appendix 1

Prudential Indicators – as at 31 December 2016

1. Ratio of Financing Costs to Net Revenue Stream

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. The definition of financing costs is set in the Prudential Code.

Ratio of Financing Costs to Net Revenue Stream	2016/17 Estimate %	2016/17 Estimate (Revised) %
General Fund	0.00	0.00
Total	**0.00**	**0.00**

As the council has no external borrowing the indicator is zero, in line with what was estimated.

2. Capital Financing Requirement

The Capital Financing Requirement (CFR) measures the council's underlying need to borrow for a capital purpose.

Capital Financing Requirement	2016/17 Estimate £m	2016/17 Estimate (Revised) £m
General Fund Capital Programme	0	0
Embedded Lease (Refuse Contract)	389	330
Total CFR	**389**	**330**

The council's underlying need to borrow for the main capital expenditure activity is nil. The embedded lease element is due to the accounting treatment (required by the Code of Practice) of the underlying assets held by Kier in delivering the refuse contract on behalf of the council.

3. Incremental Impact of Capital Investment Decisions

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax.

Incremental Impact of Capital Investment Decisions	2016-17 Estimate £	2016-17 Estimate (Revised) £
Increase in Band D Council Tax	0.50	0.32

This shows the impact of the capital investment in terms of potential increase in the Council Tax funding requirement, i.e. the opportunity costs (interest receivable) of not being able to investment these surplus funds.

4. Authorised Limit and Operational Boundary for External Debt

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).

The **Operational Boundary** links directly to the council's estimates of the CFR and estimates of other cashflow requirements

Authorised Limit for External Debt	2015/16 Approved £'000
Borrowing	2,000
Other Long-term Liabilities	450
Total	**2,450**
Operational Boundary for External Debt	
Borrowing	0
Other Long-term Liabilities	450
Total	**450**

In the unlikely event that the council would be required to borrow within the Authorised Limit and Operational Boundary, it could only be for short term rather than a long term capital investment plan.

5. Summary

The council is maintaining an affordable and sustainable capital programme in the medium term.

The council does not currently have any external debt and has not breached either the operational or authorised limits as set out in the 2016/17 Treasury Strategy.