Agenda Item 6.

East Northamptonshire Council

Finance Sub-Committee – 8 May 2017

Treasury Management Report to 31 March 2017

Purpose of report

The purpose of this report is to note the current position for Treasury Management for the period to 31 March 2017 in financial year 2016/17.

Attachment(s)

Appendix 1: Prudential Indicators – as at 31 March 2017

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 0.6% and the 4th quarter growth of 0.7%, but 1st quarter 2017 is expected to ease back.

At its meeting of 19th January, the European Central Bank (ECB) left its main policy for interest rates at -0.4%. The current €80bn monthly purchase will be reduced to €60bn from April 2017. Quarterly GDP growth rose from 0.4% in quarter 3 to 0.5% in quarter 4 of 2016. The easing in monetary policy in the euro area over the past few years has reduced the interest rates facing households and companies, and so has been one factor supporting GDP growth.

The Federal Reserve in February decided to keep interest rates on hold following its first meeting since President Donald Trump took office and the uncertain international backdrop. Despite the positive outlook on the economy, the central bank signalled there would be further gradual interest increases. Quarterly US GDP growth fell from 0.9% in quarter 3 to 0.5% in quarter 4 2016 which largely reflected the unwinding of an erratic boost in net trade in quarter 3.

2.2 **Inflation:** The Consumer Prices Index (CPI) inflation rose to 1.6% in December and further substantial increases are very likely over the coming months. In the central projection, conditioned on market yields that are somewhat higher than in November, inflation is expected to increase to 2.8% in the first half of 2018, before falling back gradually to 2.4% in three years' time. Inflation is judged likely to return to close to the target over the subsequent year. Measures of inflation compensation derived from financial markets have stabilised at around average historical levels, having increased during late 2016 as concerns about a period of unusually low inflation faded.

2.3 **Monetary Policy:** On 1 February 2017 the Monetary Policy Committee (MPC) voted unanimously in favour of maintaining the bank rate at 0.25% and re-enforcing its commitment to maintain the Quantitative Easing (QE) programme at £435bn. All Committee members judged it appropriate to leave the stance of monetary policy unchanged. The MPC noted that the path of monetary policy would continue to depend on the evolution of prospects for demand, supply, the exchange rate and therefore inflation. As a result, monetary policy could move in either direction to ensure a sustainable return of CPI inflation to the 2% target.

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

	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20
Bank rate	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.25%	0.50%	0.50%	0.75%	0.75%	0.75%
5yr PWLB rate	1.40%	1.60%	1.60%	1.70%	1.70%	1.70%	1.80%	1.80%	1.90%	1.90%	2.00%	2.00%	2.00%
10yr PWLB rate	2.10%	2.30%	2.30%	2.30%	2.40%	2.40%	2.40%	2.50%	2.50%	2.60%	2.60%	2.70%	2.70%
25yr PWLB rate	2.70%	2.90%	3.00%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.40%
50yr PWLB rate	2.50%	2.70%	2.80%	2.80%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%

3. Treasury Management Activity

3.1. During the 2016/17 financial year, the opportunity for the council to invest its surplus cash for periods beyond 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.

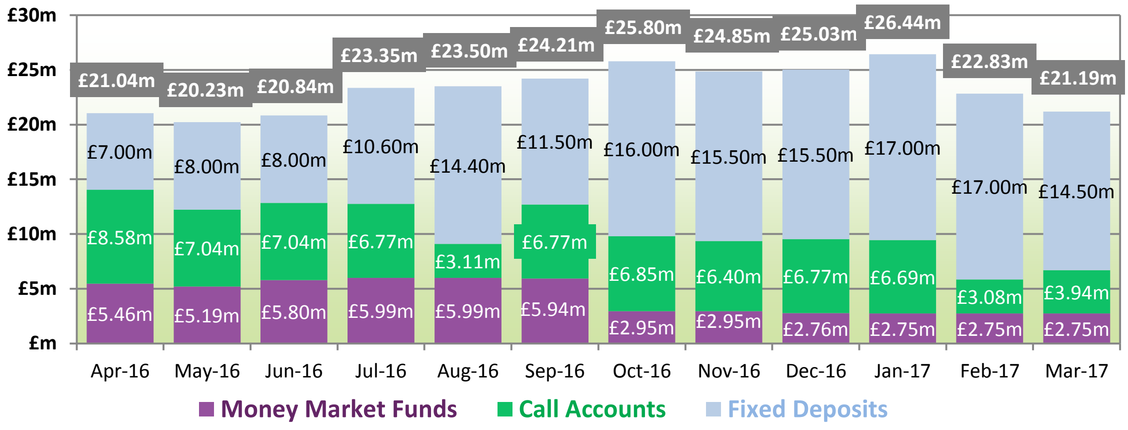
3.2. Investing for shorter durations reduces the counterparty risk the council is exposed to and the potential yield (interest rate) the council can achieve. However, since the impact of the EU Referendum vote and the Bank of England's decision to reduce interest rates earlier in the financial year, 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 rates have declined 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 March 2017.

Total amount invested March 2017



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.

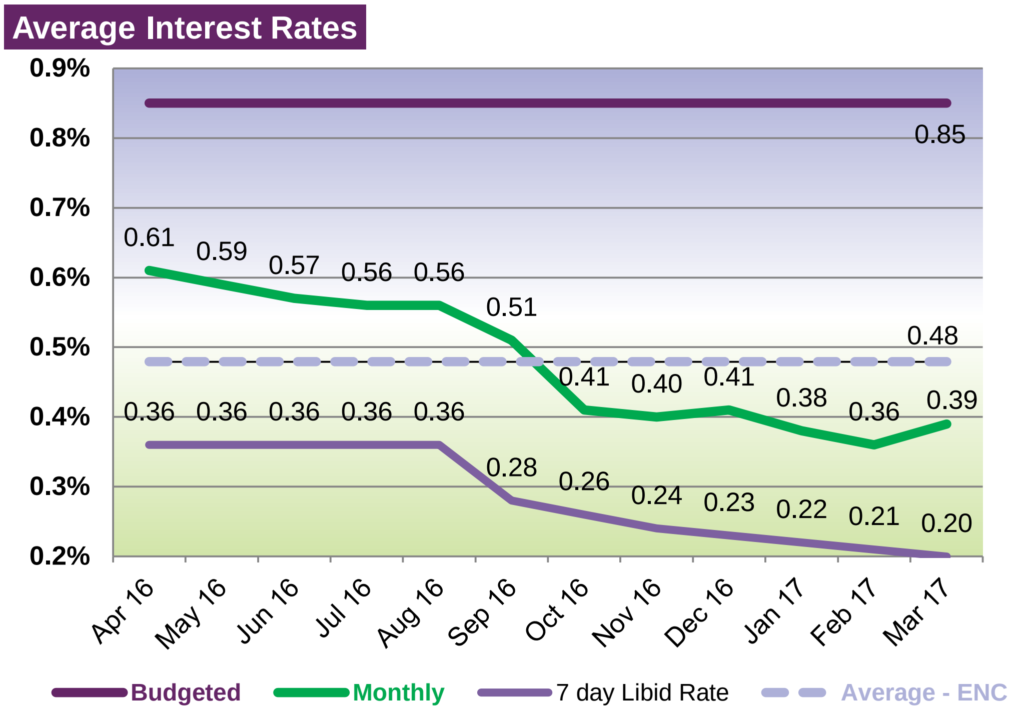
4. Treasury Management Position and Performance

4.1. The table below summarises the council's current portfolio of investments as at 31 March 2017.

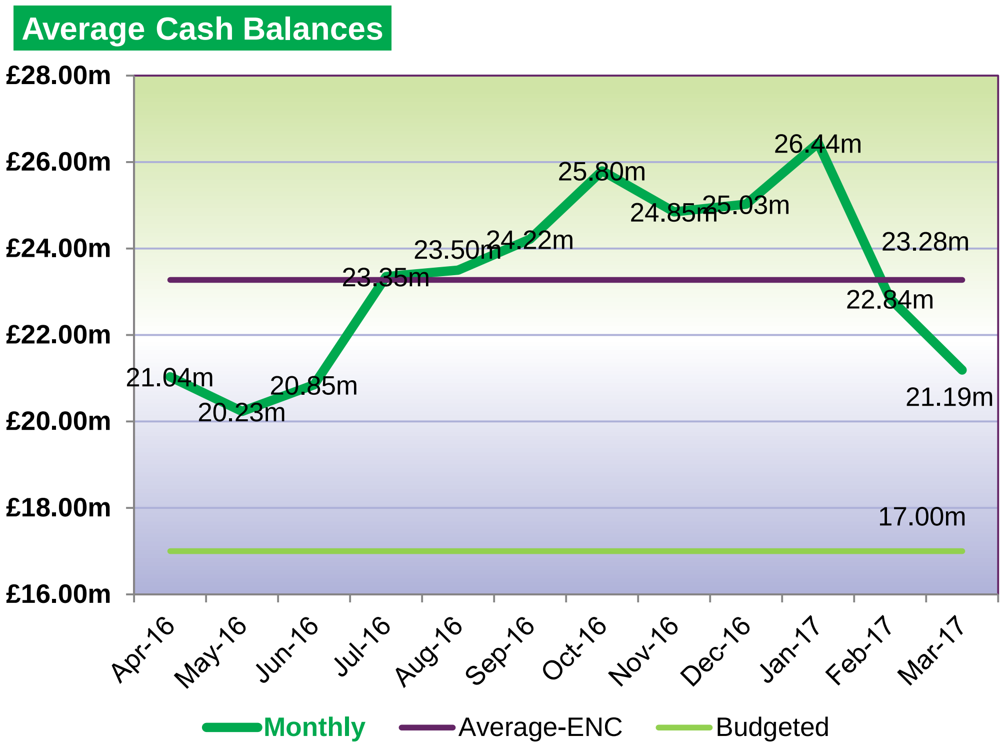
Counterparty / Lender	Amount	Rate %	Maturity Date
Call Accounts			
Santander UK (95 Day notice)	£1,500,000	0.65	
Santander UK (180 Day notice)	£1,500,000	0.90	
Barclays Bank Current Account	£935,461	0.05	
Money Market Funds			
Federated Sterling Liquidity Fund (Money Market Fund)	£2,754,626	0.29	
Fixed Term Deposits			
Coventry Building Society	£3,000,000	0.38	11/07/2017
Lloyds Bank	£1,000,000	0.45	19/06/2017
Lloyds Bank	£2,000,000	0.65	25/04/2017
Cornwall Council	£4,000,000	0.30	28/04/2017
Kingston Upon Hull City Council	£1,500,000	0.35	28/04/2017
Nationwide Building Society	£3,000,000	0.42	04/07/2017
	£21,190,087		

The average return on the council's portfolio to 31 March 2017 is 0.48%. This is 0.28% above the average 7-day London Interbank Bid Rate (LIBID) of 0.20%.

4.2. 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:



4.3. Whilst the council's investments are achieving lower rates of return, the level of cash balances held by the council remains 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.



4.4. 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 £34.9k.

4.5. 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.

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

Treasury Management Budget vs. Estimated Outturn				
	Budget	Estimated Outturn	Pressure	
	£	£	£	
Investments	£144,500	£109,580	(£34,920)	Lower interest rates being achieved, partly offset by higher than expected cash balances
Total	**£144,500**	**£109,580**	**(£34,920)**	

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 0.48% 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	£1,066,428
Increase in Band D Council Tax	0.50p	0.14p

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 to 31 March 2017 in financial year 2016/17;

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

<table>
<tr><td rowspan="2">Legal</td><td colspan="5">Power: Local Government Finance Act 2002</td></tr>
<tr><td colspan="5">Other considerations:</td></tr>
<tr><td colspan="6">Background Papers:</td></tr>
<tr><td colspan="6">Person Originating Report: Michelle Drewery, Finance Manager, 01832 742267
mdrewery@east-northamptonshire.gov.uk</td></tr>
<tr><td colspan="6">Date: 25/04/2017</td></tr>
<tr><td>CFO
25/4/17</td><td></td><td>MO</td><td></td><td>CX
25/4/17</td><td>D. Oliver</td></tr>
</table>

Appendix 1

Prudential Indicators – as at 28 February 2017

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	0.14

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	2016/17 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.