

AGENDA ITEM NO. 9

COUNCIL

Date **19 DECEMBER 2013**

Title **TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY MID-YEAR REVIEW 2013/14**

1. PURPOSE/SUMMARY

The purpose of this report is to review the Council’s Treasury Management activity for the first six months of 2013/14.

2. KEY ISSUES

- The Treasury Management Mid-Year Review 2013/14 as considered by Cabinet on 19 December 2013 and by Corporate Governance Committee on 3 December 2013 is attached.
- The report highlights all the key activities carried out within the Treasury Management function during the first six months of 2013/14. All activities have been conducted in accordance with the approved strategy and policies.
- The Capital Financing Requirement (CFR) prudential indicator has been revised.
- 2013/14 continues to be a challenging year and the report highlights the success in maximising investment income whilst ensuring the security and liquidity of the Council’s investments.

3. RECOMMENDATION

It is recommended that:-

- (i) Members note the report.

It is recommended by Cabinet and Corporate Governance Committee that:-

- (ii) The increase in the CFR prudential indicator (paragraph 4) be approved.

AGENDA ITEM NO.6**CORPORATE GOVERNANCE COMMITTEE****Date** 3 DECEMBER 2013**Title** TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY MID-YEAR REVIEW 2013/14**2. PURPOSE/SUMMARY**

The purpose of this report is to review the Council's Treasury Management activity for the first six months of 2013/14.

4. KEY ISSUES

- The Council has operated within its Treasury Management Strategy Statement (TMSS), Annual Investments Strategy and treasury limits and prudential indicators set by Council for the first six months of 2013/14.
- The Capital Financing Requirement (CFR) prudential indicator has been revised.
- Interest rates have continued at historically low rates throughout this year.
- Investment income received for the first six months of 2013/14 is £143k (£158k to end of October). The 2013/14 budgeted outturn of £210k is projected to be achieved.
- Overall interest rate achieved from investments for the first six months of 2013/14 was 1.40% (benchmark 7 day LIBID un compounded rate is 0.36%).

5. RECOMMENDATION**It is recommended that:-**

- (i) Members note the report.

It is recommended to Council that:-

- (ii) The increase in the CFR prudential indicator (paragraph 4) be approved.

Wards Affected	All
Forward Plan Reference No. (if applicable)	Not applicable
Portfolio Holder(s)	Cllr Alan Melton, Leader and Portfolio Holder, Policy and Resources and Strategic Finance Cllr Michael Humphrey, Portfolio Holder, Finance

Report Originator	Rob Bridge, Corporate Director and Chief Finance Officer Mark Saunders, Chief Accountant
Contact Officer(s)	Rob Bridge, Corporate Director and Chief Finance Officer Mark Saunders, Chief Accountant
Background Paper(s)	Capita Asset Services template Cabinet Report 21 February 2013 General Fund Budget 2013/14 and Capital Programme 2013/16

1. INTRODUCTION

- 1.1. Treasury management is defined as “The management of the local authority’s investments and cash flows, its 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.”
- 1.2. The Council complies with the requirements of The Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice 2011.
- 1.3. The primary requirements of the Code are as follows:
 - Creation and maintenance of a Treasury Management Policy Statement, which sets out the policies and objectives of the Council’s treasury management activities.
 - Creation and maintenance of Treasury Management Practices, which set out the manner in which the Council will seek to achieve those policies and objectives.
 - Receipt by full Council of an annual Treasury Management Strategy Statement – including the Annual Investment Strategy and Minimum Revenue Provision Policy – for the year ahead, a mid-year Review Report and an Annual Report covering activities during the previous year.
 - Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
 - Delegation by the Council of the role of scrutiny of treasury management strategy and policies (including Mid-year Review Report) to a specific named body. For this Council the delegated body is: Corporate Governance Committee.
- 1.4. This mid-year report has been prepared in compliance with CIPFA’s Code of Practice on Treasury Management and covers the following:
 - an economic update for the first six months of 2013/14;
 - a review of the Treasury Management Strategy Statement and Annual Investment Strategy;
 - the Council’s capital position;
 - a review of the Council’s investment portfolio for 2013/14;
 - a report of the Council’s borrowing strategy for 2013/14;
 - a report of debt rescheduling during 2013/14;
 - a review of compliance with Treasury and Prudential Limits for 2013/14.

2. ECONOMIC UPDATE

- 2.1. During 2013/14 economic indicators suggested that the economy is recovering, though from a low level. After avoiding recession in the first quarter of 2013, with a 0.3% quarterly expansion the economy grew 0.7% in Q2. There have been signs of renewed vigour in household spending in the summer, with a further increase in retail sales, mortgages, house prices and new car registrations.
- 2.2. The strengthening in economic growth appears to have supported the labour market, with employment rising at a modest pace and strong enough to reduce the level of unemployment further. Excluding bonuses, earnings rose by just 1.0% y/y, well below the rate of inflation at 2.7% in August, causing continuing pressure on household's disposable income.
- 2.3. The Bank of England extended its Funding for Lending Scheme (FLS) into 2015 and sharpened the incentives for banks to extend more business funding, particularly to small and medium size enterprises. The mortgage market still appears to have been the biggest beneficiary from the scheme, with mortgage interest rates falling further to new lows. Together with the Government's Help to Buy Scheme, which provides equity loans to credit constrained borrowers, this is helping to boost demand in the housing market. Mortgage approvals by high street banks have risen as have house prices, although they are still well down from the boom years of pre 2008.
- 2.4. The public borrowing figures continued to be distorted by a number of one offs factors. On an underlying basis, borrowing in Q2 started to decrease, but only slowly as Government expenditure cuts took effect and economic growth started to show through in a small increase in tax receipts. The 2013 Spending Review, covering only 2015/16, made no changes to the headline Government spending plan and monetary policy was unchanged in advance of the new Bank of England Governor, Mark Carney arriving. Bank Rate remained at 0.5% and quantitative easing also stayed at £375bn. In August the Monetary Policy Committee (MPC) provided guidance that Bank Rate is unlikely to change until unemployment first falls to 7%, which is not expected until mid 2016. However, 7% is only the point at which the MPC will review Bank Rate, not necessarily take action to change it.
- 2.5. Consumer Price Index inflation (MPC target of 2.0%), fell marginally from a peak of 2.9% in June to 2.7% in August. The Bank of England expects inflation to fall back to 2.0% in 2015.
- 2.6. Tensions in the Eurozone eased over the second quarter but there remained a number of triggers for a renewed flare up. Economic survey data improved consistently over the first half of the year, pointing to a return to growth in Q2, so ending six quarters of Eurozone recession.
- 2.7. The overall balance of risks to economic recovery in the UK is now weighted to the upside after five months of robust good news on the economy. However, only time will tell just how long this period of strong economic growth will last and it remains exposed to vulnerabilities in a number of key areas. The longer run trend is for gilt yields and Public Works Loan Board (PWLB) rates to rise, due to the high volume of gilt issuance in the UK and bond issuance in other major western countries.
- 2.8. Prospects for interest rates and borrowings over the medium term are shown below.

	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17
Bank rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%
5yr PWLB rate	2.50%	2.50%	2.50%	2.60%	2.70%	2.70%	2.80%	2.80%	2.90%	3.00%	3.20%	3.30%	3.50%	3.60%	3.70%
10yr PWLB rate	3.70%	3.70%	3.70%	3.70%	3.80%	3.80%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.60%	4.60%
25yr PWLB rate	4.40%	4.40%	4.40%	4.40%	4.50%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.10%	5.10%	5.20%
50yr PWLB rate	4.50%	4.40%	4.40%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%	5.20%	5.20%	5.30%

3. TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY UPDATE

3.1. The Treasury Management Strategy Statement (TMSS) for 2013/14 was approved by the Council on 21 February 2013. The increase in the Capital Financing Requirement (CFR) detail in paragraph 4.5 below is the only change to the TMSS since February.

4. THE COUNCIL'S CAPITAL POSITION

4.1. This part of the report is structured to update:

- the Council's capital expenditure plans;
- how these plans are being financed;
- the impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- compliance with limits in place for borrowing activity.

4.2. This table shows the revised estimates for capital expenditure and financing of the capital programme and the changes since the budget was approved.

Capital Programme	2013/14 Original Estimate £000	2013/14 Revised Estimate £000
Forecast Capital Expenditure (including capital expenditure financed by leases)	3,586	3,171
Financed by:		
Capital Receipts	850	875
Capital Grants	390	685
Capital Reserves	2,346	1,331
Total Financing	3,586	2,891
Net Financing Need For The Year (increase in CFR)	0	280

4.3. The main change to the capital programme since it was last approved is the

reprofiling of expenditure and capital resources between years.

- 4.4. The table below shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period; this is termed the Operational Boundary.

Prudential Indicators	2013/14 Original Estimate £000	2013/14 Revised Estimate £000
Capital Financing Requirement	355	635
External Debt / Operational Boundary		
Borrowing	10,000	10,000
Other Long Term Liabilities Finance Leases	2,000	2,000
Total Debt 31 March	12,000	8,217

- 4.5. The Council's revised estimate for CFR is £280k higher than the original estimate. This reflects the decision to bring forward the leasing of two refuse vehicles from 2014/15 to 2013/14. Whilst this increases the CFR and therefore the Council's borrowing requirement, this type of lease includes a borrowing facility and so the Council is not required to separately borrow to fund these leases. The Council has made provision to repay this lease liability in the General Fund revenue budget.
- 4.6. Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within defined limits. One of these is that the Council needs to ensure that its gross debt, does not, except in the short term, exceed the total CFR in the preceding year plus the estimates of any additional CFR for 2013/14 and the next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent.

Limits to Borrowing Activity	2013/14 Original Estimate £000	2013/14 Revised Estimate £000
Gross Borrowing	7,800	7,800
Plus Other Long Term Liabilities Finance Leases	320	417
Gross Borrowing	8,120	8,217
Capital Financing Requirement	355	635

- 4.7. As a result of the Council's long term Public Works Loan Board (PWL) debt portfolio of £4.5m (31/03/13) currently attracting excessive premiums (£2.5m at the time of writing this report) if it were prematurely repaid, it is not financially advantageous for the Council to fully comply with this prudential indicator.

- 4.8. A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit, which represents the limit beyond which borrowing is prohibited and needs to be set and revised by Members. It reflects the level for borrowing which, while not desired could be afforded in the short term but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Authorised Limit for External Debt	2013/14 Original Estimate £000	2013/14 Revised Estimate £000
Borrowing	15,000	15,000
Plus Other Long Term Liabilities Finance Leases	2,000	2,000
Total Borrowing	17,000	17,000

- 4.9. The Corporate Director & Chief Finance Officer reports that no difficulties are envisaged for the current year in complying with the above prudential indicators.

5. INVESTMENT PORTFOLIO

- 5.1. In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity and to obtain an appropriate level of return which is consistent with the Council's risk appetite. As set out in section 2, it is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the 0.5% bank rate. The introduction of the Funding for Lending Scheme has reduced market investment rates even further. The potential for a prolonging of the Eurozone sovereign debt crisis and its impact on banks, prompts a low risk and short term strategy. Given this risk environment, investment returns are likely to remain low.
- 5.2. The Council held investments of £20.10m as at the 30 September 2013 (£14.85m at 31 March 2013) and the investment portfolio yield for the first 6 months of the year is 1.40% against a benchmark (7 day LIBID un compounded rate) of 0.36%.
- 5.3. The Chief Finance Officer confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2013/14. The Council has achieved investment income of £143k to 30 September 2013 (£158k to end of October). The 2013/14 budgeted outturn of £210k is projected to be achieved.
- 5.4. The Council's current investment counterparty criterion was approved in the TMSS in February 2013 and has met the requirements of the treasury management function to date.
- 5.5. The Council creditworthiness policy is based on a sophisticated modeling approach supported by Capita Asset Services (the Council's treasury management advisors), the basis of which utilises credit ratings from the three credit ratings agencies- Fitch, Moody's and Standard and Poors. This credit rating information is supported by addition information including credit default swaps and other market information.

6. BORROWING STRATEGY

- 6.1. No new borrowing has been undertaken in the first six months and none is anticipated during the remainder of this financial year, as stated in the TMSS report approved by Council on 21 February 2013.

7. DEBT RESCHEDULING

- 7.1. Debt rescheduling opportunities have been limited in the current economic climate and consequent structure of interest rates. No debt rescheduling was undertaken during the first six months of 2013/14.