

TELFORD & WREKIN COUNCIL

AUDIT COMMITTEE – 30 JUNE 2015

TREASURY MANAGEMENT - 2014/15 ANNUAL REPORT AND 2015/16 TO DATE

REPORT OF THE ASSISTANT DIRECTOR: FINANCE, AUDIT & INFORMATION GOVERNANCE (CHIEF FINANCIAL OFFICER)

PART A) – SUMMARY REPORT

1. SUMMARY OF MAIN PROPOSALS

The report updates members on the outcome of Treasury Management activities for 2014/15 and details the position for 2015/16 to date.

2014/15 Treasury Outturn

The treasury portfolio ended the year with net indebtedness of £112.8m (borrowing: £116.6m less investments: £3.8m). Base rate was 0.5% for the whole year and is predicted to stay at 0.5% until 2016.

The borrowing strategy for 2014/15 was to use maturing investments to reduce borrowing, where possible. Borrowing was £9m lower at 31 March 2015 compared to 31 March 2014, however investments were £19.8m lower due to the use of maturing investments to reduce the need for borrowing in line with the strategy. The net increase in net indebtedness was due to capital expenditure. Short term borrowing was used to fund short term cash flow requirements during the year at favourable interest rates generating a significant benefit for the Council's budget.

The investment strategy for 2014/15 was to gain maximum benefit with security of capital being the key consideration. The average return on investments for the year was 0.92% against a benchmark of 0.44%.

Overall, treasury delivered a net over-achievement of £2.149m against the budget set for 2014/15. The majority of the saving relates to the benefit of extending the change in the calculation of the Minimum Revenue Provision applied in 2013/14 to include supported debt (government allocations), which is made up of a back-dated element of £1.1m and an ongoing benefit of £0.3m. It also includes £0.246m generated as a one-off saving in 2014/15 as a result of capitalisation of interest on capital projects pending their completion.

2015/16 Update

The strategy for 2015/16 remains consistent with that of the previous year. Investment opportunities will be reviewed as they arise and we will seek to gain maximum benefit within the agreed risk parameters. There are currently no long term investments, which reduces counter-party risk and also reduces net interest costs as longer-term borrowing costs tend to be greater than we are able to earn on new investments.

Based on the capital programme, borrowing will be required during the year and consideration will be given to the maturity profile of current debt, interest rates and refinancing risks as well as the source, which is primarily expected to be the Public Works Loans Board.

We will also seek to identify any further potential one-off or ongoing treasury management savings opportunities such as further reviews of the Council's MRP policies.

Temporary borrowing was £28m at 31/3/15 and has increased slightly to £28.5m as at 31 May 2015. Investments were £11m at 31 May 2015.

2. RECOMMENDATIONS

Audit Committee Members are asked to:-

- 2.1 note the contents of the report
- 2.2 note the performance against Prudential Indicators.

3. *SUMMARY IMPACT ASSESSMENT*

COMMUNITY IMPACT	Do these proposals contribute to specific priority plan objectives? Yes/ No Efficient Community Focussed Council Will the proposals impact on specific groups of people? Yes/ No
TARGET COMPLETION / DELIVERY DATE	Part of ongoing Treasury Management Activities within the Treasury Management Strategy and Policy approved by Council.
FINANCIAL/VALUE FOR MONEY IMPACT	Yes/ No Where appropriate these are detailed in the body of the report.
LEGAL ISSUES	Yes/ No The AD: Finance, Audit and IG (Section 151 Officer), has responsibility for the administration of the financial affairs of the Council. In providing this report the Section 151 Officer is meeting one of the responsibilities of the post contained within the Council's Constitution at Part 2, Article 12, paragraph 12.04(f) which states "The Chief financial Officer will contribute to the

promotion and maintenance of high standards of governance, audit, probity and propriety, risk management and the approval of the statement of accounts through provision of support to the Audit Committee.”

**OTHER IMPACTS,
RISKS AND
OPPORTUNITIES**

Yes/No

The key opportunities and risks associated with treasury management activities are set out in the body of the report and in the Treasury Management Strategy and Policy approved by Council and will be regularly monitored throughout the year.

**IMPACT ON
SPECIFIC WARDS**

Yes/No

4. **PREVIOUS MINUTES**

Council 27 February 2014

Audit Committee 30 June 2014

Audit Committee 27 January 2015

Council 5 March 2015

PART B – ADDITIONAL INFORMATION

5. **BACKGROUND**

Treasury Management in local government is regulated by the 2001 revision of the CIPFA Treasury Management in Public Services: Code of Practice (the Code). This Council has adopted the Code and fully complies with its requirements. The primary requirement of the Code is the formulation and agreement by full Council of a Treasury Policy Statement, which states the policies and objectives of its treasury management activities.

A requirement of the Council’s Treasury Management Practices is the reporting to the Council of both the expected treasury activity for the forthcoming financial year (the annual treasury strategy statement) and subsequently the results of the Council’s treasury management activities in that year (this annual treasury report).

6. **2014/15**

The annual report is covered in paragraphs 6-15 and deals with: -

- 2014/15 Portfolio position;
- the borrowing strategy for 2014/15;
- the borrowing outturn for 2014/15;
- compliance with treasury limits;
- investments strategy for 2014/15;
- investments outturn for 2014/15;
- debt rescheduling;
- Shropshire Council debt
- overall outturn position

- leasing

7. 2014/15 PORTFOLIO POSITION

The Council's treasury management position at the beginning and the end of the year was as follows: -

	31 March 2014		31 March 2015	
	Principal £m	Rate %	Principal £m	Rate %
Borrowing	125.583	3.37	116.613	3.49
Investments	23.510	3.38	3.778	0.92
Net Indebtedness	(102.073)		(112.835)	

There was new temporary borrowing and repayment of £11m PWLB during 2014/15; temporary borrowing was £28.1m at 31 March 2015. The capital programme was funded from a combination of borrowing, capital receipts, grants and other external contributions plus funds from maturing investments; this has resulted in an increase in net indebtedness during the year. Prudential borrowing increased in 2014/15 due to planned capital expenditure approved as part of the capital programme.

The Adopted Treasury Strategy was to:-

- Monitor borrowing opportunities determined by the prevailing markets.
- To use maturing investments to reduce borrowing where possible.
- Reduce the volatility of investment returns while maintaining adequate flexibility in arrangements.
- To achieve optimum return on investments commensurate with proper levels of security and liquidity.

9. COUNCILS RESPONSE TO ECONOMIC CLIMATE

- 9.1 Political uncertainty had a large bearing on market confidence this year. These included the Scottish referendum, the concerns over Greece and the run up to the general election. Base rate remained at 0.5% throughout the whole of 2014/15. The UK economy showed growth of 3% in 2014. Annual inflation fell to 0% in March, having been 1.6% a year earlier. Base rate has generally been predicted to stay at 0.5% until mid 2016.
- 9.2 The Council has reduced both the amount and duration of its investments. These funds were used to reduce the need to borrow and reduce exposure to investment risk.
- 9.3 We have closely followed guidance issued by our Treasury Advisors in relation to credit ratings, financial standing and duration.

10. **BORROWING 2014/15**

10.1 **Original Economic Projections**

The Expectation for Interest Rates – When the budget was set for 2014/15 the “average” City view anticipated that Bank Rate would remain at 0.5% until mid 2015 before starting to rise gradually back towards more normal levels in 2015, though Bank Rate would take a long time to return to around 4.5%.

10.2 **Outturn 2014/15**

During 2014/15 the Monetary Policy Committee (MPC) was focused on helping the economy to recover, but with inflation falling to target level.

The MPC also maintained the level of quantitative easing at £375bn.

The dominant focus in 2014/15 was on quarterly GDP growth figures and the unemployment rate. Overall for 2014/15 the economy grew by 3%.

Inflation had been a major concern of the MPC but this has fallen from 1.6% in March 2014 to 0.0% in March 2015. Inflation is predicted to increase back to the 2% target level within the 2 year horizon.

Borrowing and Investment Rates in 2014/15

The overnight investment rate has varied little during the year.

Treasury Borrowing and Rescheduling

The borrowing strategy for the current year has been to use maturing investments to reduce the Council’s exposure to interest and market volatility and reduce borrowing where possible.

During the year we borrowed no new PWLB loans, although we did have some maturities totalling £11m.

PWLB Repayments & Discounts

No loans were repaid early or rescheduled during the year.

An analysis of the maturity structure of our debt is shown below. The maturing in less than 1 year includes £1.001m of PWLB loans.

Analysis of Debt Maturity as at 31st March

	2014		2015	
	£'000	%	£'000	%
Maturing in less than 1 year	37,063	29.5	29,093	25.0
Maturing in 1-2 years	1,001	0.8	1,001	0.9
Maturing in 2-5 years	3,002	2.4	3,003	2.6
Maturing in 5-10 years	1,506	1.2	507	0.4
Maturing in more than 10 years*	<u>83,011</u>	66.1	<u>83,009</u>	71.1
	<u>125,583</u>	100.0	<u>116,613</u>	100.0

* this includes £60m LOBO (Lenders Option Borrowers Option) loans that are potentially callable at certain points before the maturity date. There is therefore the potential that these loans would have to be replaced sooner exposing the council to the prevailing market at that time. To-date, none of our LOBOs have been called before maturity.

Debt Performance

As highlighted in section 7 the average debt portfolio rate has risen over the course of the year from 3.37% to 3.49%. This is due to less temporary borrowing being undertaken in 2014/15 as compared to 2013/14. The low rates of this in 2013/14 led to a slightly lower interest rate of the portfolio in that year.

11. COMPLIANCE WITH TREASURY LIMITS

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

12. INVESTMENTS 2014/15

12.1 Strategy

Internally Managed Investments - The authority currently manages all of its investments in-house and invests within the institutions complying with its counterparty limits and credit ratings. Some investments are short term related to cash flows and others include longer term investment instruments that benefited returns in 2014/15.

Investment Strategy - The agreed short term investment strategy for 2014/15 was to achieve optimum return on investments commensurate with proper levels of security and liquidity and to use maturing investments to reduce the need to borrow, where possible.

12.2 Outturn 2014/15

Detailed below are the results of the investment strategy undertaken by the Council, based on the average investment during the year.

	Average Investment	Rate of Return (gross of fees)	Rate of Return (net of fees)	Benchmark Return *
<u>Internally Managed</u>				
Investments	£24.214m	0.92%	0.92%	0.44%

No institutions in which investments were made showed any difficulty in repaying investments and interest in full during the year.

13. SHROPSHIRE COUNCIL DEBT

The Council makes an annual contribution (£1.877m in 2014/15) towards County Council costs on pre disaggregation debt (i.e. pre unitary inception) - interest paid averaged 5.49% last year. The rate of interest paid on this is managed by Shropshire and is considerably

higher than the rate payable by Telford & Wrekin Council on its borrowing.

14. **OVERALL OUTTURN FOR 2014/15**

The net overall position is summarised in the table below. The sound overall position has resulted from a mix of cash flow benefits plus proactive treasury management activities. The budget reflected the position when the budget was set, the underspend has been achieved through active management of debt principal and the low interest rates prevailing for the year. Overall a net saving of just over £2.1m was made against budget for the year which is summarised below:

Summary of Outturn Position

	Estimate £m	Outturn £m	Variance £m
Interest Received	(0.3)	(0.2)	0.1
Principal Repayments	4.6	4.3	(0.3)
MRP saving from change of policy	0.0	(1.4)	(1.4)
Contribution to provision	0.0	0.1	0.1
Capitalisation of Interest	(0.0)	(0.2)	(0.2)
Interest Paid	<u>5.3</u>	<u>4.9</u>	<u>(0.4)</u>
Net Position	9.6	7.5	(2.1)

15. **LEASING**

Each year the Council arranges operating leases for assets such as vehicles, computers and equipment. This helps spread the cost over a number of years in line with the anticipated life of the equipment.

The final drawdown for 2014/15 was completed in March. The drawdown consisted of an operating lease from Siemens totalling £0.033m and funded the purchase of ICT equipment over three years and a finance lease with JCB Finance totalling £0.299m and funded the purchase of ICT equipment at an interest rate of 1.34%.

16. **2015/16 UPDATE**

The remainder of this report deals with the current financial year based largely on information to 31 May 2015.

16.1 **Strategy**

The strategy for 2015/16 is to continue to keep investments as short term, where possible, to reduce the need to borrow thus reducing investment exposure and maximising overall returns to the revenue account. We will review investment opportunities if they arise and also review borrowing opportunities as we progress through the year and look to take advantage of the advantageous interest rates if possible. 2015/16 and 2016/17 will see the Council investing in significant regeneration projects including building homes and commercial property for rent as part of the approved Housing Investment Programme

16.2 **Interest Rates**

Base rate began the year at 0.5% and has remained there. The current expectation is that there will be no increase before mid 2016.

16.3 **Prudential Regime**

This Council agreed its required indicators at Council on 5 March 2015. There have been no breaches of the indicators and none have been amended. The Council set itself an Operational limit for external debt of £370m for 2015/16 and an Authorised limit of £390m. Our total borrowing outstanding (including PFI) is £171m which is within both limits.

16.4 **Borrowing**

We have not taken any new borrowing in 2015/16 and have had no maturities to-date. In total we have £1m maturing during 2015/16.

16.5. **Internally Managed Investments**

The strategy for the year is to gain maximum benefit at minimum risk whilst achieving as a minimum, the 7 day deposit rate. As mentioned above, we will also continue to use maturing investments, where possible, to reduce the need to borrow. For the period to 31 May 2015 some £438m worth of investments have been made in our overnight call accounts. Rates have ranged from 0.35% to 0.40%. As at 31 May 2015 internal investments stood at £11.41m.

Potentially the Council can place up to £20.0m with any Counterparty. At the end of May the greatest exposure with a single counterparty was £10.0m with Svenska Handelsbanken (87.7% of the portfolio). It was also our only investment with a non UK sovereign institution. A detailed breakdown is shown in Appendix 2.

16.6 **Non UK Sovereign Counterparty Limits**

At present we have a non UK sovereign counterparty limit set at £20m.

17 **Background Papers**

CIPFA Code of Practice for Treasury Management in Local Authorities;
Fund Manager Valuations; Temporary Borrowing records; PWLB
records
Investment records

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PRUDENTIAL INDICATORS

PRUDENTIAL INDICATOR	2013/14	2014/15	2014/15
(1). EXTRACT FROM BUDGET AND RENT SETTING REPORT	£m	£m	£m
	Actual Outturn	Original Estimate	Actual Outturn
Capital Expenditure			
TOTAL	84.6	115.7	115.3
Ratio of financing costs to net revenue stream			
General fund	3.11%	3.85%	3.85%
Net borrowing requirement			
brought forward 1 April	110.6	125.6	125.6
carried forward 31 March	125.6	108.3	116.6
in year borrowing requirement	+15.0	-17.3	-9.0
Capital Financing Requirement as at 31 March			
TOTAL	271.1	270.3	295.5
Annual change in Cap. Financing Requirement			
TOTAL	+29.1	-5.6	+19.6
Incremental impact of capital investment decisions	£ p	£ p	£ p
Increase in council tax (band D) per annum (not cumulative)	-3.71	21.20	21.20

PRUDENTIAL INDICATOR	2013/14	2014/15	2014/15
(2). TREASURY MANAGEMENT PRUDENTIAL INDICATORS	£m	£m	£m
	final	original	final
Authorised limit for external debt -			
borrowing	145	170	240
other long term liabilities	65	64	64
TOTAL	210	234	304
Operational boundary for external debt -			
borrowing	125	158	223
other long term liabilities	63	62	62
TOTAL	188	220	285
Upper limit for fixed interest rate exposure			
Net principal re fixed rate borrowing / investments	100	100	100
Upper limit for variable rate exposure			
Net principal re variable rate borrowing / investments:-	80%	80%	80%
Upper limit for total principal sums invested for over 364 days			
(per maturity date)	95%	95%	95%

Maturity structure of fixed rate borrowing during 2014/15	lower limit	upper limit
under 12 months	0%	40%
12 months and within 24 months	0%	25%
24 months and within 5 years	0%	50%
5 years and within 10 years	0%	75%
10 years and above	25%	100%

Summary of Investments at 31 May 2015

	Sovereign Credit Rating	Individual credit Rating	Total £m	%
Call Accounts				
HSBC	UK AA+	F1+AA- support 1 viability a+	1.413	12.4
Svenska Handelsbanken	SWE AAA	F1+AA- support 2 viability aa-	10.000	87.6
			11.413	100.0
Fixed Deposits				
			0	
			0.000	0.0
Variable Deposit				
			0	
Total			34.968	100.0
Non UK holding £10m (Limit £20m)				