
Report To:	Policy & Resources Committee	Date:	17th November 2015
Report By:	Chief Financial Officer	Report No:	FIN/107/15/JB/KJ
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Subject:	TREASURY MANAGEMENT – MID-YEAR REPORT 2015/16		

1.0 PURPOSE

- 1.1 The purpose of this report is to advise Members of the operation of the treasury function and its activities for the first six months of 2015/16 as required under the terms of Treasury Management Practice 6 ("TMP6") on "Reporting Requirements and Management Information Arrangements".

2.0 SUMMARY

- 2.1 As at 30 September 2015 the Council had gross external debt (including PPP) of £281,397,134 and investments of £52,983,197. This compares to gross external debt (including PPP) of £284,125,698 and investments of £44,787,396 at 31 March 2015. The reduction in external debt is due to the repayment of external debt and reduction in PPP debt.
- 2.2 The Council is projected to be underborrowed by £24,048,000 compared to its Capital Financing Requirement as at 31 March 2016. This is an increase of £3,563,000 in underborrowing from the estimated position in the 2015/16 Treasury Management Strategy of £20,485,000. The Council has undertaken no borrowing so far in 2015/16 and no borrowing is projected for the remainder of the year.
- 2.3 The average rate of return achieved on investments during the first six months of 2015/16 was 0.73% which exceeds the benchmark return rate for the year of 0.45% by 0.28% and resulted in £71,600 of additional interest on investments for the Council.
- 2.4 During the first six months of 2015/16 the Council did not undertake any debt restructuring and operated within the required treasury limits and Prudential Indicators for the year set out in the Council's Treasury Policy Statement, annual Treasury Strategy Statement, and the Treasury Management Practices.

3.0 RECOMMENDATIONS

- 3.1 It is recommended that the Committee notes the contents of the Mid-Year Report on Treasury Management for 2015/16 and the ongoing work to ensure the delivery of financial benefits for the Council.
- 3.2 It is also recommended that the Mid-Year Report be remitted to the Full Council for approval.

Alan Puckrin
Chief Financial Officer

4.0 BACKGROUND

- 4.1 The Council is required by the CIPFA Code of Practice on Treasury Management 2011 and the CIPFA Prudential Code for Capital Finance in Local Authorities to produce a mid-year treasury management review of activities and prudential and treasury indicators for 2015/16.
- 4.2 Treasury Management in this context is defined as: “The management of the local authority’s 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.”
- 4.3 A glossary of treasury management terms is attached as Appendix 1.

5.0 MID-YEAR REVIEW

- 5.1 The treasury management issues arising during the first six months of 2015/16 were:
 - a. The Council’s debt (excluding PPP) has reduced during the period by £0.645m due to repaying maturing debt without undertaking new borrowing.
 - b. The Council’s investments have increased by £8.196m during the period due to increased cash flow and timing of income.
 - c. As at 31 March 2015 the Council had under borrowed against its capital financing requirement by £19.255m. The latest projection is for this under borrowing to increase to £24.048m at 31 March 2016. Under borrowing means that the Council is using funds it currently has to cash flow capital expenditure rather than bringing in new funds from borrowing. The projected level of under borrowing is considered manageable but the position is kept under review in light of Council capital financing and other funding requirements.
 - d. No borrowing has been undertaken during 2015/16 to date and no borrowing is projected for the year.
 - e. The Council did not undertake any debt restructuring during the first six months of 2015/16 and remained within its Prudential Indicator and Treasury Management limits during the year.
 - f. The Bank Rate remained unchanged during the period at 0.50% (unchanged since March 2009). The first increase is now forecast by the Council’s treasury advisers for Quarter 2 of 2016 although this increase may be delayed due to ongoing economic uncertainty.
 - g. PWLB rates for new borrowing were expected to increase by between 0.20% and 0.30% during the period. Rates have increased but only by around 0.10% although volatility during the period led to spreads between high and low rates of up to 0.66% for some loan periods. The Council’s treasury advisers expect PWLB rates to increase further during the rest of the year but the extent and speed of increase will depend on economic factors affecting the UK and global markets.
 - h. Investment returns were expected to remain relatively low and this was indeed the position during the period.
 - i. The Council’s investments earned a rate of return of 0.73% during the period and outperformed the benchmark return of 0.45% resulting in additional income to the Council of £71,600.
 - j. All investments were in accordance with the Council’s investment policy and no institutions with which investments were made had any difficulty in repaying those investments and interest in full during the period.
 - k. The Council’s investment performance is due to undertaking fixed term investments at interest rates that were above the benchmark with a counterparty which has high creditworthiness (the Bank of Scotland) and in accordance with the Council’s investment strategy.

5.2 As advised in the Treasury Management Annual Report for 2014/15, the UK Government are continuing with their trading plan to sell their shares in the Lloyds Banking Group which includes the Bank of Scotland who are the Council's bankers and with whom the Council has regularly undertaken fixed term deposits. The removal of government ownership does not affect the strength or stability of the Bank but may cause the Council to reduce the maximum period for investments with the Bank under the Investment Strategy and affect the likely return on any fixed-term funds invested with the Bank.

5.3 The Council's debt position was as follows:

	At 31 March 2015	At 30 September 2015
	£	£
Total Excluding PPP	214,314,698	213,670,134
PPP Debt	69,811,000	67,727,000
Total Including PPP	284,125,698	281,397,134

Further detail is given in the following table:

	At 31 March 2015		At 30 September 2015		Movement In Period
	Principal	Rate	Principal	Rate	Principal
	£000		£000		£000
Fixed Rate Funding:					
- PWLB	111,373		110,730		(643)
- Market *	36,000		36,000		See * Below
	147,373	3.95%	146,730	3.92%	(643)
Variable Rate Funding:					
- PWLB	0		0		0
- Market *	66,900		66,900		See * Below
- Temporary	42		40		(2)
	66,942	4.81%	66,940	4.81%	(2)
Total Debt (Excl PPP)	214,315	4.22%	213,670	4.20%	(645)
PPP Debt	69,811		67,727		(2,084)
Total Debt (Incl PPP)	284,126		281,397		(2,729)

* - Market Loans are shown as variable when they have less than 1 year to go until their next call date. The total value of Market Loans has not changed between financial years, just the split between fixed and variable.

5.4 The Council's investment position was as follows:

	At 31 March 2015		At 30 September 2015		Movement In Period
	Principal	Return	Principal	Return	Principal
	£000		£000		£000
Investments:					
- Fixed Term Deposits	32,500	0.85%	32,500	0.79%	0
- Deposit Accounts	12,287	0.50%	20,483	0.50%	8,196
Totals	44,787	0.76%	52,983	0.68%	8,196

Maximum level of investments in Period: £58,087,597 on 17 September 2015

Minimum level of investments in Period: £45,961,697 on 28 April 2015

Daily average for the period: £51,130,655.

5.5 2015/16 Latest Projection Compared to Estimates in 2015/16 Strategy

The latest 2015/16 projection compared to the estimates in the 2015/16 strategy:

	2015/16 Estimate	2015/16 Latest Projection
<u>Borrowing Requirement</u>	£000	£000
New borrowing	0	0
Alternative financing requirements	0	0
Replacement borrowing	0	0
TOTAL	0	0
<u>Prudential/Treasury Management Indicators</u>		
	£000	£000
Gross external debt including PPP (As at 31 March 2016)	280,864	280,852
Capital financing requirement (As at 31 March 2016)	301,349	304,900
(Under)/over borrowing against CFR	(20,485)	(24,048)
	£000	£000
Net external borrowing and capital financing requirement (As at 31 March 2016)	(54,135)	(61,143)
	£000	£000
Capital expenditure	29,486	32,992
• Capital Programme		
• PPP Schools/Finance Leases (incl. accounting adjustments)	(1,904)	(2,084)
Total	27,582	30,908
Ratio of financing costs (including PPP/ Finance Leases) to net revenue stream	11.90%	11.90%
Incremental impact of capital investment decisions - incremental increase in council tax (band D) per annum (use of capital receipts and prudential borrowing for capital expenditure)	£1.00	£1.06

5.6 2015/16 Mid-Year Position Compared to Limits in 2015/16 Strategy

The 2015/16 mid-year position compared to limits in the 2015/16 strategy:

	2015/16 Limits	2015/16 Mid-Year Position
<u>Prudential/Treasury Management Indicators</u>		
Authorised limit for external debt	£000	£000
• Borrowing	239,000	213,670
• Other long term liabilities	68,000	67,727
	307,000	281,397
Operational boundary for external debt		
• Borrowing	234,000	213,670
• Other long term liabilities	68,000	67,727
	302,000	281,397
Upper limit for fixed interest rate exposure	140%	91%
Upper limit for variable rate exposure	40%	9%
Upper limit on sums invested for periods longer than 364 days (Actual is maximum in period)	£000 10,000	£000 0
Limits on fixed rate borrowing maturing in each period (LOBOs included based on call dates and not maturity dates) at 31 March 2016		
• Under 12 months	45%	3.7%
• 12 months and within 24 months	45%	11.2%
• 24 months and within 5 years	45%	34.6%
• 5 years and within 10 years	45%	17.2%
• 10 years and within 30 years	45%	6.0%
• 30 years and within 50 years	45%	27.3%
• 50 years and within 70 years	45%	0.0%
<u>Council Policy Limits</u>		
Maximum Percentage of Debt Repayable In Year	25%	18.7%
Maximum Proportion of Debt At Variable Rates	40%	31.3%
Maximum Percentage of Debt Restructured In Year	30%	0.0%

The forecast Investment Balances for 2015/16 required under Investment Regulation 31 and the actual position at 30 September 2015 is shown in Appendix 2. An analysis of the cash balances managed in-house is shown in Appendix 3.

5.7 The forecast from the Treasury Advisors in the Strategy for the Bank Rate as at 31 March and the latest forecast are:

	Forecast Per 2015/16 Strategy	Latest Forecast
2015/16	0.75%	0.50%
2016/17	1.25%	1.00%
2017/18	2.00%	1.75%

- 5.8 The Council's investment policy for the year is governed by Scottish Government Investment Regulations, which was implemented in the annual investment strategy approved by the Council on 9 April 2015. This policy sets out the approach for choosing investment categories and counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data such as rating outlooks, credit default swaps, bank share prices etc.
- 5.9 All investments were in accordance with the policy and no institutions with which investments were made had any difficulty in repaying investments and interest in full during the year.

The result of the investment strategy undertaken by the Council in the first six months of 2015/16 is as follows:

Average Investment	Rate of Return (gross of fees)	Benchmark Return (3 month LIBID uncompounded)
£51,131,000	0.73%	0.45%

The Council have outperformed the benchmark by 0.28% resulting in additional income to the Council of £71,600. Opportunities for the Council to out-perform the benchmark rate are becoming fewer due to more standardisation of rates and periods offered.

6.0 IMPLICATIONS

Legal

- 6.1 None. Any borrowing or lending is done under the Council's legal powers.

Finance

Through the achievement of exceeding the investment benchmark return rate, the Council has benefited from additional returns of £71,600. The Council utilises Treasury Management as part of the overall Financial Strategy. Officers will continue to investigate borrowing and investment opportunities to bring financial benefits to the Council, all within the Treasury Management Policy.

Human Resources

- 6.2 None.

Equalities

- 6.3 None.

Repopulation

- 6.4 None.

7.0 CONSULTATIONS

- 7.1 This report has been produced based on advice from the Council's treasury advisers (Capita Treasury Solutions Limited).

8.0 LIST OF BACKGROUND PAPERS

- 8.1 CIPFA - Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes – 2011 Edition
Inverclyde Council – Treasury Management Strategy 2015/16.

TREASURY MANAGEMENT
GLOSSARY OF TERMS

Authorised Limit for External Debt

This is a limit for total Council external debt as set by the Council based on debt levels and plans.

Bank of England

The central bank for the UK with ultimate responsibility for setting interest rates (which it does through the Monetary Policy Committee or “MPC”).

Bank Rate

The interest rate for the UK as set each month by the Monetary Policy Committee (“MPC”) of the Bank of England. This was previously referred to as the “Base Rate”.

Call Date

A date on which a lender for a LOBO loan can seek to apply an amended interest rate to the loan. The term “call date” is also used in relation to some types of investments with a maturity date where the investments can be redeemed on call dates prior to the maturity date.

Capital Expenditure

Expenditure on or for the creation of fixed assets that meets the definition of Capital Expenditure under the accounting rules as set-out in the Code of Practice on Local Authority Accounting in the United Kingdom and for which the Council are able to borrow.

Capital Financing Requirement

The Capital Financing Requirement (sometimes referred to as the “CFR”) is a Prudential Indicator that can be derived from the information in the Council’s Balance Sheet. It generally represents the underlying need to borrow for capital expenditure (including PPP schemes).

CIPFA

CIPFA is the Chartered Institute of Public Finance and Accountancy who produce guidance, codes of practice, and policy documents for Councils.

Counterparty

Another organisation involved in a deal i.e. if the Council enters a deal with a bank then the bank would be referred to as the “Counterparty”.

Credit Ratings

Credit ratings are indicators produced by a ratings provider (such as Fitch, Moody's or Standard & Poor's) that aim to give an opinion on the relative ability of a financial institution to meet its financial commitments. Credit ratings are not guarantees – they are opinions based on investigations and assessments by the ratings providers and they are regularly reviewed and updated. The Council makes use of credit ratings to determine which counterparties are appropriate or suitable for the Council to make deposits with.

The highest credit rating is AAA.

European Central Bank

Sometimes referred to as “the ECB”, the European Central Bank is the central bank for the Eurozone and is the equivalent of the Bank of England. The European Central Bank sets interest rates for the Eurozone.

Eurozone

This is the name given to the group of 19 countries in Europe that have the Euro as their currency and that participate in a monetary union. Interest rates in the Eurozone are set by the European Central Bank. The Eurozone is comprised of: Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia, and Spain.

Federal Reserve

Sometimes referred to as “the Fed”, the Federal Reserve is the central bank for the US and is the equivalent of the Bank of England. The Federal Reserve sets interest rates for the US.

Fixed Term Deposit

A Fixed Term Deposit or Fixed Term Investment is an investment with a named bank or financial institution which matures on a set date and which is repaid with interest on the maturity date. Fixed Term Deposits cannot be traded and cannot be terminated before the maturity date without the payment of a penalty (if at all).

Gilt Yields

A gilt yield is the effective rate of return that someone buying a gilt at the current market price will receive on that gilt. Since the market price of a gilt can vary at any time, the yield will also vary.

Gilts

Gilts are bonds (i.e. debt certificates) that are issued (i.e. sold) by the UK Government. When they issue gilts the Government sets the interest rate that applies to the gilt, sets when they will repay the value of the gilt, and it agrees to make interest payments at regular intervals until the gilt is repaid or redeemed. Gilts are traded in the financial markets with the price varying depending on the interest rate applicable to the gilt, when the gilt will be repaid (i.e. when it will mature), on Bank Rate expectations, and on market conditions.

Gross Domestic Product

Gross Domestic Product (“GDP”) is a measure of the output of goods and services from an economy.

Growth

Positive growth in an economy is an increase in the amount of goods and services produced by that economy over time. Negative growth in an economy is a reduction in the amount of goods and services produced by that economy over time.

Incremental Impact of Capital Investment Decisions

These are Prudential Indicators that reflect the impact on Council Tax of movements in projected and estimated capital expenditure within and between financial years.

Inflation

Inflation is the term used for an increase in prices over time. It can be measured in various ways including using the Consumer Prices Index (“CPI”) or the Retail Prices Index (“RPI”).

Investment Regulations

The Local Government in Scotland Act 2003 allows the Scottish Ministers to introduce Regulations to extend and govern the rules under which Scottish Councils may invest funds. The Local Government Investments (Scotland) Regulations 2010 came into effect on 1st April 2010.

LIBID

This is the London Interbank Bid Rate – an interest rate that is used between banks when they wish to attract deposits from each other.

LIBOR

This is the London Interbank Offering Rate – an interest rate that is used as a base for setting interest rates for deals between banks.

LOBO

This is a form of market loan that the Council has with some lenders. The term is short for the phrase “Lender Option/Borrower Option”.

MPC

The MPC or Monetary Policy Committee is a committee of the Bank of England that meets each month (in a meeting over 2 days) to set the Bank Rate for the UK.

Operational Boundary

This is a level of debt set by the Council at lower than the Authorised Limit and which Council debt levels should not normally exceed during normal operations.

Prudential Code

Councils are required to comply with the CIPFA Prudential Code for Capital Finance in Local Authorities. These requirements include the production of Prudential Indicators. The Prudential Code was last revised in November 2011.

Prudential Indicators

Indicators set-out in the Prudential Code that will help Councils to meet requirements in relation to borrowing limits or which will help Councils demonstrate affordability and prudence with regard to their prudential capital expenditure.

PWLB

The Public Works Loan Board is a government agency and part of the Debt Management Office. The PWLB provides loans to local authorities and other specified bodies.

PWLB Certainty Rates

In the Budget in March 2012, the Chancellor of the Exchequer announced that local authorities that provide information on their long-term borrowing and capital spending plans would be eligible for a 0.20% discount rate for new PWLB borrowing. The PWLB Certainty Rates came into effect on 1st November 2012.

PWLB Rates

These are the interest rates chargeable by the Public Works Loan Board for loans. The rates for fixed rate loans are determined by the day on which the loan is agreed. The rates to be charged by the PWLB for loans are set each day based on gilt yields at the start of business each day and then updated at least once during the day.

Quantitative Easing

This is the creation of money by a central bank (such as the Bank of England) in order to purchase assets from banks and companies and boost the supply of money in an economy.

Spread

For interest rates the spread is the difference between the highest and lowest rate for that interest rate over a period.

Treasury Management Code

This is the "Treasury Management in the Public Services: Code of Practice" and is a code of practice for Council treasury management activities. It is produced by CIPFA and was last revised in November 2011.

Treasury Management Indicators

These are Prudential Indicators specifically relating to Treasury Management issues.

Treasury Management Practices (TMPs)

This is a Council document that sets out Council policies and procedures for treasury management as required by the Treasury Management Code. The Council also agrees an annual treasury management strategy that is submitted to Committee in accordance with the Treasury Management Practices.

Yield

The yield is the effective rate of return on an investment.

**FORECAST OF INVESTMENT BALANCES
ESTIMATE FOR 2015/16 AND ACTUAL AT 30 SEPTEMBER 2015**

Investment Regulation 31 requires the Council to provide forecasts for the level of investments. The estimate for 2015/16 and the actual as at 30 September 2015 are:

	2015/16	2015/16
	Estimate For Year	Actual For 1 April 2015 to 30 September 2015
	£000	£000
Cash balances managed in-house		
- At Start of Year	50,169	49,467
- At End of Year/Period	33,650	52,983
- Change in Year/Period	(16,519)	3,516
- Average daily cash balances	41,910	51,131
Holdings of shares, bonds, units (includes local authority owned company)		
- At Start of Year	2	2
- Purchases	0	0
- Sales	0	0
- At End of Year/Period	2	2
Loans to local authority company or other entity to deliver services		
- At Start of Year	0	0
- Advances	600	124
- Repayments	10	0
- At End of Year/Period	590	124
Loans made to third parties		
- At Start of Year	2,240	2,240
- Advances	1,803	11
- Repayments	33	17
- At End of Year/Period	4,010	2,234
Total of all investments		
- At Start of Year	52,411	51,709
- At End of Year/Period	38,252	55,343
- Change in Year/Period	(14,159)	3,634

**CASH BALANCES MANAGED IN-HOUSE
ACTUAL AS AT 1 APRIL 2015 AND 30 SEPTEMBER 2015**

The following is an analysis of cash balances managed in-house as at 1 April 2015 and at 30 September 2015:

	As At 1 April 2015	As At 30 September 2015
	£	£
<u>Fixed Term Deposits</u>		
Bank of Scotland	22,500,000	22,500,000
Nationwide Building Society	10,000,000	10,000,000
	32,500,000	32,500,000
Average Interest Rate	0.85%	0.79%
<u>Deposit Accounts</u>		
Bank of Scotland	12,286,900	20,482,700
Santander UK	496	497
	12,287,396	20,483,197
Average Interest Rate	0.50%	0.50%
TOTAL	44,787,396	52,983,197
Average Interest Rate	0.76%	0.68%