Report of	Meeting	Date
Chief Executive	Governance Committee	25 January 2017

TREASURY MANAGEMENT ACTIVITY TO 31 DECEMBER 2016

PURPOSE OF REPORT

1. To report on Treasury Management performance and compliance with Prudential Indicators in financial year 2016/17 to the end of December.

RECOMMENDATION(S)

2. That the report be noted.

EXECUTIVE SUMMARY OF REPORT

3. Average interest earned is 0.30% to the end of December. As in 2015/16, cash balances have been used as a source of internal borrowing to minimise external borrowing at higher rates of interest, thereby achieving revenue budget savings.

4. Updated Capital Expenditure and Capital Financing Requirement Prudential Indicators will be presented in the Treasury Strategy report to Full Council on 28 February 2017. The report will also be presented to the Governance Committee meeting of 22 March 2017.

Confidential report Please bold as appropriate	Yes	**No**

CORPORATE PRIORITIES

5. This report relates to the following Strategic Objectives:

Involving residents in improving their local area and equality of access for all		A strong local economy	
Clean, safe and healthy communities		An ambitious council that does more to meet the needs of residents and the local area	

BACKGROUND

6. Special Council of 1 March 2016 approved the Treasury Management Policy Statement; Treasury Management Practices; Prudential Indicators for 2016/17 to 2018/19; the Treasury Management Strategy and Treasury Indicators for 2016/17; the Annual Investment Strategy 2016/17; and the Annual Minimum Revenue Provision (MRP) Policy for 2016/17.

7. The Treasury Management Annual Report for 2015/16 was presented to Governance Committee of 22 June 2016.

8. The Code of Practice for Treasury Management requires Councils to review their treasury strategies and activities half yearly. This report satisfies that requirement.

PRUDENTIAL INDICATORS

Capital Expenditure and Capital Financing Requirement (CFR) 2016/17

9. The Prudential Indicators reported on 1 March 2016 took account of estimated capital expenditure and sources of financing from 2015/16 to 2018/19. These will be updated in the Treasury Strategy report to be presented to Full Council on 28 February 2017, and will add financial year 2019/20 and will take account of any rephasing of expenditure between financial years, adjustments to financing, and the addition of any projects to the capital programme. The report will also be presented to Governance Committee's meeting of 22 March 2017.

The CFR and Borrowing 2016/17

10. The Prudential Code requires that borrowing net of investments should not exceed the CFR for the preceding year plus any anticipated increase in the current and next two years. This is in order to ensure that Councils borrow only for capital investment purposes. As at 31 March 2016, net borrowing as reported in the Treasury Management Annual Report 2015/16 was £13.478m and therefore was well below the CFR of £34.497m at the same date. Net borrowing will not exceed the CFR in 2016/17, and the actual year-end figure will be confirmed in the Treasury Management Annual Report for the financial year.

11. As there is a large margin between net borrowing and the CFR, the Council could take additional external borrowing should it need to top-up cash balances. However, there would be a "carrying cost" of additional borrowing, because the interest rates payable would exceed the interest rates receivable on the cash balances. As indicated in Table 1 below, the average rate of interest earned this year to December is 0.30%, whereas interest payable on new PWLB loans would be 1.35% (5 years) to 2.45% (50 years) (see Appendix C). Even though there would be a "carrying cost" of taking additional PWLB loans, this may prove necessary to achieve savings in the longer run if significant increases in interest rates on borrowing became imminent.

Operational Boundary for External Debt 2016/17

12. The Operational Boundary for external debt should reflect the most likely, but not worst case, scenario consistent with the Council's approved budgets. Gross borrowing and other long-term liabilities should not exceed the Operational Boundary. The figure approved on 1 March 2015 was £39.200m, being the forecast gross borrowing and other long-term liabilities as at 31 March 2017. Actual borrowing at that date is expected to be lower, because as much as possible of the CFR is matched by internal rather than external borrowing. Use for internal borrowing is the most effective use of the Council's cash balances while available, and so far in 2016/17 no new long-term external borrowing has been taken. The Operational Boundary was set at a value based on the CFR to allow additional external borrowing should cash balances be depleted, without breaching the Prudential Indicator.

Authorised Limit 2016/17

13. The Authorised Limit should allow headroom above the Operational Boundary to accommodate the fluctuations that can occur in cash flows. The figure approved for 2016/17 was £42.200m, and there is no reason to amend this at present.

Ratio of Financing Costs to the Revenue Stream 2014/15

14. The Ratio of Financing Costs to the Revenue Stream shows the percentage of the Council's income from Government grants and council tax that has been used to meet interest costs and debt repayment. The actual figure for 2016/17 will be presented in the Treasury Management Annual Report 2016/17 in June 2017.

Incremental Impact of Capital Investment Decisions 2016/17

15. The Incremental Impact of Capital Investment Decisions measures the cumulative impact of capital expenditure on the revenue budget. It is not possible to make a meaningful comparison against this indicator other than when it is restated in the annual Treasury Strategy, which will be presented to Council in February 2017.

TREASURY ACTIVITY

16. Investment activity up to the end of December 2016 is summarised in the following table.

Table 1 - Investment Activity	**Average Daily Investment £'000**	**Earnings to 31/12/16 £**	**Average Rate %**
Fixed Term Deposits	-	-	-
Call Accounts	2,231	4,545	0.27
Money Market Funds	2,436	6,067	0.33
Total	**4,667**	**10,612**	**0.30**

Compared to 2015/16, the main change has been the lower balance available to invest, which means that it has not been possible to invest for longer periods in order to achieve higher interest rates. Cash balances would have been higher had additional long-term borrowing been taken in order to finance capital expenditure. This would have generated sufficient cash to allow investment in fixed term deposits at higher interest rates. However, in recent months the rates offered for 3 or 6 month deposits have declined, to the extent that 0.60% for a six months deposit would be considered a good rate, depending on the availability of other counterparties. The interest rates on any loans taken would have been considerably higher than this, probably in excess of 3% for 25 to 50-year loans, so there would have been a cost of carry.

A full list of current investments is shown below.

Table 2 - Investments as at 31 December 2016					
Counterparty	**Type**	**Amount £**	**Rate %**	**Invested date**	**Maturity date**
Standard Life	MMF	3,000,000	variable	Various	On call
Federated	MMF	1,500,000	variable	Various	On call
Barclays	Call account	271,551	0.20	Various	On call
Total		**4,771,551**			

There are no changes proposed to the current list of Financial Institutions and Investment Criteria.

17. The average interest earned of 0.30% does not exceed the benchmark of 0.35% (being the average LIBID 7 day rate). The reason is that cash balances have not been available to permit investments in term deposits at higher rates of interest than available for call accounts or money market funds (MMFs). In general a term deposit of 3 or 6 months would offer a higher rate of interest than is available for deposits in call accounts or MMFs. In addition the rate offered by MMFs has continued to reduce, because the rates offered by banks to the MMFs have reduced in recent months, so that cash in the funds has been reinvested at lower rates than were available earlier in the year.

18. The Council's treasury advisors, Capita Asset Services, have provided a detailed commentary on interest rate forecasts, which is presented as Appendix B. Bank rate and PWLB borrowing rate forecasts are given from September quarter 2016 through to March quarter 2020. Appendix C shows the current Capita forecast and the forecast rates included in the Treasury Strategy in March 2016. Compared to the previous interest rates forecast, PWLB rates are currently lower than expected, and are not considered likely to increase by as much by March quarter of 2018 as had previously been suggested.

19. An increase in Bank rate from 0.50% to 0.75% was expected in the March quarter of 2017. Instead the rate reduced to 0.25%, and it is expected to remain at this level until the June quarter of 2019. An increase to 0.75% is currently considered possible in the December quarter of 2019, over two years later than the previous forecast.

TREASURY CONSULTANTS' ADVICE

20. Appendix A presents the advice of Capita Asset Services' economic research consultants Capital Economics in respect of economic matters up to the third quarter of 2016/17. In addition, a detailed commentary on interest rate forecasts is presented as Appendix B.

21. Capita's suggested budgeted investment earning rates for investments up to about three months duration in each financial year for the next seven years are as follows:

Average Earnings in each financial year		
	Revised December 2016	**Original March 2016**
2016/17	0.25%	0.60%
2017/18	0.25%	1.25%
2018/19	0.25%	1.75%
2019/20	0.50%	2.00%
2020/21	0.75%	2.25%
2021/22	1.00%	2.50%
2022/23	1.50%	2.75%
2023/24	1.75%	2.75%
Later years	2.75%	3.00%

22. The most recent estimate is compared to the estimated earnings rate available at the time the Treasury Management Strategy was presented for approval in March 2016. Clearly the suggested earnings rates are lower now than before the start of the financial year. The average rate to 31 December on the council's cash investments has exceeded the Capita suggested target for the financial year, though not by a large margin.

IMPLICATIONS OF REPORT

23. This report has implications in the following areas and the relevant Directors' comments are included:

Finance	✓	Customer Services	
Human Resources		Equality and Diversity	
Legal		Integrated Impact Assessment required?	
No significant implications in this area		Policy and Communications	

COMMENTS OF THE STATUTORY FINANCE OFFICER

24. This report complies with statutory requirements. Statistical content is consistent with the assumptions in the approved capital and revenue budgets for 2016/17, including changes approved during the year.

COMMENTS OF THE MONITORING OFFICER

25. The Monitoring Officer has no comments.

GARY HALL
CHIEF EXECUTIVE

There are no background papers to this report.

Report Author	Ext	Date	Doc ID
Michael Jackson	5490	16 January 2017	Treasury Management Activity to 31 December 2016.docx