Report of	Meeting	Date
Chief Finance Officer	Governance Committee	21 June 2017

TREASURY MANAGEMENT ANNUAL REPORT 2016/17

PURPOSE OF REPORT

1. To report on Treasury Management performance and compliance with Prudential Indicators for the financial year ended 31 March 2017.

RECOMMENDATION(S)

2. That the report be noted.

EXECUTIVE SUMMARY OF REPORT

3. This report advises on compliance with Prudential and Treasury Indicators in 2016/17. The return on investments for the year was 0.29%, which exceeded the benchmark of 0.24%. Details of borrowing and investments as at 31 March 2017 are presented.

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

CORPORATE PRIORITIES

4. 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

5. The current regulatory environment concerning treasury management places a greater onus on members to scrutinise treasury policy and activity. To enable that, each year the Council is required to consider, as a minimum, three treasury reports. These consist of an annual strategy statement in advance of the year (Council 1 March 2016), a mid-year review of that strategy (Governance Committee 25/1/2017), and finally this out-turn report.

6. Revised Prudential and Treasury Indicators for 2016/17 were included in the report "Treasury Strategies and Prudential Indicators 2017/18 to 2019/20", presented to Special Council of 28 February 2017. Where relevant, comparisons with 2016/17 indicators in this report are to those approved most recently.

PRUDENTIAL INDICATORS

7. Prudential Indicator: Capital Expenditure and Financing 2016/17

The Council's 2016/17 Capital Programme has been reported to Executive Cabinet and Council at intervals during the year. An analysis of capital expenditure in the year and variances from budgets, including rephasing of expenditure to 2016/17, is given in the report "Provisional Revenue and Capital Outturn 2016/17", being presented to the Executive Cabinet meeting of 22 June 2017.

In summary, capital expenditure for 2016/17 (including Revenue Expenditure Funded from Capital Under Statute, and land acquired by exchange) was £11.037m, compared to the estimate of £14.563m when the prudential indicator for the year was revised. Financing of capital expenditure in 2016/17, and the impact on the Capital Financing Requirement, is shown in the table below.

8. Prudential Indicator: Capital Financing Requirement 2016/17

The Capital Financing Requirement is a measure of the capital expenditure incurred by the Council which still has to be paid for. Financing of such expenditure is by a combination of external borrowing, generally loans from the Public Works Loan Board (PWLB), or temporary use of internal cash balances. Ultimately the expenditure has to be paid for and will be a charge to Council Tax payers. The Minimum Revenue Provision (MRP) charged to the Council's revenue budget each year is based on the CFR. Its impact on reducing the CFR is shown in the following table.

The revised CFR estimated for 2016/17 was £39.544m; therefore the actual CFR of £39.287m is £0.257m less than estimated.

	2015/16 £'000	**2016/17 £'000**
Opening Capital Financing Requirement	33,200	34,497
Capital investment		
Property, Plant and Equipment	2,232	9,897
Intangible Assets	0	12
Heritage Assets	99	44
Revenue Expenditure Funded from Capital under Statute	1,688	1,084
Total Capital Investment including REFFCUS	4,019	11,037
Sources of finance		
Capital Receipts	(185)	(141)
Capital Receipts - exchanged land	0	(2,490)
Government Grants and Other Contributions	(1,125)	(2,264)
Sums set aside from revenue		
Revenue Financing	(874)	(758)
Minimum Revenue Provision – statutory	(490)	(522)
Capital receipts applied to reduce CFR	(48)	(72)
Closing Capital Financing Requirement	**34,497**	**39,287**
Explanation of movements in year		
Increase in prudential borrowing	1,835	5,384
Provision made for debt repayment	(538)	(594)
Increase/(Decrease) in Capital Financing Requirement	**1,297**	**4,790**

9. Prudential Indicator: The CFR and Borrowing

In order to ensure that local authorities borrow only for capital purposes, 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 the next two years.

Total borrowing at 31 March 2017 was £18.537m (excluding accrued interest), £11.537m of which was from PWLB, and £7.000m was temporary borrowing from other local authorities.

Cash balances (net of bank overdraft) invested at year-end were £0.955m (excluding accrued interest receivable), which meant that borrowing net of investments was £17.582m. This was lower than the estimated net figure of £24.115m because additional PWLB loans to finance new capital investment or to replace internal borrowing were not taken.

The net borrowing figure is £21.705m less than the Capital Financing Requirement quoted above, this figure representing the use of the Council's own cash to finance capital expenditure rather than taking additional external loans.

When the treasury strategy for 2016/17 was approved, it was anticipated that the interest rate for a 25-year PWLB loan would rise to 3.50% by the March quarter of 2017, and that the rate would continue to rise to 3.80% by the March quarter of 2019. Based on the expected interest rate increase, estimated borrowing for the financial year assumed that new external loans would be taken to replace use of internal cash before rates were increased, as well as to finance new capital investment projects during the year. This would have a 'carrying cost' in the short-term, because interest payable would exceed interest earned on the additional cash balance that would become available to invest; but it would have achieved savings in the longer term by borrowing before rates increased.

In practice, the likelihood of an immediate increase in rates diminished during 2016/17, and use of internal cash balances rather than new external loans continued. On 31 March 2017 the 25-year PWLB rate was 2.67% and there was no immediate prospect of a sharp increase. Rates will continue to be monitored, and bearing in mind the Council's capital investment plans additional external long-term borrowing will be required during 2017/18 as reflected in the current Treasury Strategy.

10. Compliance with Borrowing Limits (Operational Boundary & Authorised Limit)

The Prudential Indicators include two borrowing limits: the Operational Boundary, which reflects the expected borrowing position; and the Authorised Limit, which provided headroom to cater for unanticipated cash movements.

The revised Operational Boundary for 2016/17 was set at £27.130m, which included £27.115m external borrowing plus £0.015m other long-term liabilities. The actual total for the year was £18.553m (excluding accrued interest, but including other long-term liabilities), and the reason for the reduction was the continuing use of internal cash balances rather than external borrowing to finance capital expenditure. The prudential borrowing for the year of £5.384m was financed from internal balances. Use of internal cash balances in this way reduces the net cost of financing capital investment for the time being, though in the longer run additional external borrowing will be required.

The revised Authorised Limit was set at £30.130m, to allow a margin for temporary borrowing if required for cash management purposes. Actual borrowing and other long-term liabilities were £18.553m and therefore were below the limit.

11. Prudential Indicator: Ratio of Financing Costs to the Revenue Stream

This indicator identifies the percentage of the Council's income from Government grants, Council Tax, and the local share of business rates which has been used to meet interest costs and debt repayment (MRP). The estimate reported in the Treasury Strategy 2016/17 was 7.01%. The actual ratio was 5.61%. In calculating the actual ratio, a number of income and expenditure items have been excluded. One-off Government grants such as those relating to the December 2015 floods have been excluded, because they were not anticipated in the original estimate and therefore would have distorted the comparison. Interest received other than that earned on cash balances invested has been excluded because it was not in the estimated ratio. By excluding these non-recurring items, it is easier to focus on the reasons for the reduction in the ratio.

The main variance was in in financing costs, which were lower than estimated because the carrying cost of taking new loans to replace internal borrowing was avoided. Interest receivable was less than estimated, but interest payable was reduced by a larger value.

The Revenue Stream excludes the income from assets such as Market Walk. In practice the income from Market Walk is more than covering the financing costs, but this cannot be reflected in the Prudential Indicator.

12. Prudential Indicator: Incremental Impact of Capital Investment Decisions

This indicator is concerned with the cumulative impact on the revenue budget of capital expenditure over a number of years. It is not possible to give a meaningful comparison against this indicator, other than when it is restated each year in the Treasury Strategy.

13. Treasury Position as at 31 March 2017

	As last reported (in 2017/18 Treasury Strategy) **£'000**	**Actual value as at 31 March 2017** **£'000**
Borrowing at period start (excluding temporary borrowing for cash flow management)	12,800	12,800
Borrowing repaid in year	(1,263)	(1,263)
Borrowing in year	15,578	7,000
Total borrowing at period end **	**27,115**	**18,537**
Cash & investments **	**(3,000)**	**(955)**
** Excluding accrued interest		
Net Borrowing	**24,115**	**17,582**

Note: £7.0m borrowing was short-term for cash management purposes

14. Treasury Indicator: Upper Limit on Fixed Interest Rate Exposure

The Council is exposed to fixed interest rates on its borrowings. The upper limit on fixed interest rate exposure for 2016/17 was set at 100%, and is equivalent to the Operational Boundary. The limit was not breached.

15. Treasury Indicator: Upper Limit on Variable Interest Rate Exposure

The Council is exposed to variable interest rates on cash invested temporarily in money market funds and call accounts. The table below shows that on average £4.653m was invested each day in such funds. The upper limit on variable rate exposure for 2016/17 was set at £14m. This upper limit took account of the potential need for external borrowing to finance capital investment to replace use of internal cash balances. The effect would have been to increase cash available for investment, though at a much lower rate of interest than would have been paid on the new loans. As a consequence, no new loans were taken in 2016/17 and cash invested peaked at £11m.

16. Investments and Average Rate Achieved

The following table summarises investment activity and returns during 2016/17:

Details	Average Daily Investment £'000	Interest Earned £	Average Rate %
Money Market Funds	2,688	8,176	0.30
Call accounts	1,965	5,322	0.27
Sub Total – MMF/Call accounts	**4,653**	**13,498**	
Short Term deposits	0	0	n/a
Debt Management Office (DMO)	0	0	n/a
Total	**4,653**	**13,498**	**0.29**

The average interest earned of 0.29% exceeded the performance benchmark of 0.24%, being the 7-day London Inter-Bank Bid Rate (LIBID) plus 15%. Though use of the DMO was avoided, because the rate of interest earned is only 0.10% (compared to 0.25% in 2015/16), it was not possible to place cash balances in term deposits, which pay higher interest rates than call accounts and money market funds.

The average rate achieved in 2016/17 has reduced compared to 2015/16, when 0.44% was achieved and the 7-day LIBID was 0.40%. The likelihood is that the average rate achieved in 2017/18 will remain low, which tends to support the strategy of using internal cash balances where possible in order to minimise additional borrowing required to finance capital investment.

IMPLICATIONS OF REPORT

17. 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

18. This report meets statutory reporting requirements. Its statistical content is consistent with the Council's draft financial accounts for the financial year 2016/17.

COMMENTS OF THE MONITORING OFFICER

19. The Monitoring Officer has no comments.

GARY HALL
CHIEF EXECUTIVE & STATUTORY FINANCE OFFICER

Background Papers			
Document	**Date**	**File**	**Place of Inspection**
Treasury Strategy 2016/17 Treasury Strategy 2017/18	01/3/16 28/2/17		Town Hall

Report Author	Ext	Date	Doc ID
Michael Jackson	5490	12 June 2017	Treasury Management Annual Report 2016-17.docx