

## ANNUAL TREASURY MANAGEMENT REVIEW 2016/17

Council	<b>07 September 2017</b>
Report Author	<b>Tim Willis, Section 151 Officer</b>
Portfolio Holder	<b>Portfolio Holder for Financial Services and Estates</b>
Status	<b>For Decision</b>
Classification:	<b>Unrestricted</b>
Key Decision	<b>No</b>
Reasons for Key	<b>N/A</b>
Previously Considered by	<b>Governance and Audit Committee – 28 June 2017 Cabinet – 27 July 2017</b>
Ward:	<b>N/A</b>

### Executive Summary:

This report summarises treasury management activity and prudential/ treasury indicators for 2016/17.

### Recommendation(s):

That Council:

- Notes the actual 2016/17 prudential and treasury indicators in this report.
- Approves the Annual Treasury Management report for 2016/17.

### CORPORATE IMPLICATIONS

<b>Financial and Value for Money</b>	The financial implications are highlighted in this report.
<b>Legal</b>	Section 151 of the 1972 Local Government Act requires a suitably qualified named officer to keep control of the Council's finances. For this Council, this is the Director of Corporate Resources, Tim Willis, and this report is helping to carry out that function.
<b>Corporate</b>	Failure to undertake this process will impact on the Council's compliance with the Treasury Management Code of Practice.
<b>Equalities Act 2010 &amp; Public Sector Equality Duty</b>	There are no equity and equalities implications arising directly from this report, but the Council needs to retain a strong focus and understanding on issues of diversity amongst the local community and ensure service delivery matches these.

	It is important to be aware of the Council's responsibility under the Public Sector Equality Duty (PSED) and show evidence that due consideration had been given to the equalities impact that may be brought upon communities by the decisions made by Council.
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<b>CORPORATE PRIORITIES (tick those relevant)✓</b>	
A clean and welcoming Environment	
Promoting inward investment and job creation	
Supporting neighbourhoods	

<b>CORPORATE VALUES (tick those relevant)✓</b>	
Delivering value for money	✓
Supporting the Workforce	
Promoting open communications	

## **1.0 Introduction and Background**

- 1.1 This Council is required by regulations issued under the Local Government Finance Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2016/17. This report meets the requirements of both the Chartered Institute of Public Finance & Accountancy (CIPFA) Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).
- 1.2 During 2016/17 the minimum reporting requirements were that the full Council should receive the following reports:
- an annual treasury strategy in advance of the year (Council 04/02/2016)
  - a mid-year treasury update report (Council 09/02/2017)
  - an annual review following the end of the year describing the activity compared to the strategy (this report)
- 1.3 The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.
- 1.4 This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Governance and Audit Committee before they were reported to the full Council. Member training on treasury management issues was last undertaken on 21/09/2015 in order to support members' scrutiny role. The Council's external treasury management advisor is Capita Asset Services (Capita).
- 1.5 The Council's 2016/17 accounts have not yet been audited and hence the figures in this report are subject to change.

## 2.0 Capita's Review of the Economy and Interest Rates (issued by Capita in April 2017)

- 2.1 The two major landmark events that had a significant influence on financial markets in the 2016/17 financial year were the UK EU referendum on 23 June and the election of President Trump in the USA on 9 November. The first event had an immediate impact in terms of market expectations of when the first increase in Bank Rate would happen, pushing it back from quarter 3 2018 to quarter 4 2019. At its 4 August meeting, the Monetary Policy Committee (MPC) cut Bank Rate from 0.5% to 0.25% and the Bank of England's Inflation Report produced forecasts warning of a major shock to economic activity in the UK, which would cause economic growth to fall almost to zero in the second half of 2016. The MPC also warned that it would be considering cutting Bank Rate again towards the end of 2016 in order to support growth. In addition, it restarted quantitative easing with purchases of £60bn of gilts and £10bn of corporate bonds, and also introduced the Term Funding Scheme whereby potentially £100bn of cheap financing was made available to banks.
- 2.2 In the second half of 2016, the UK economy confounded the Bank's pessimistic forecasts of August. After a disappointing quarter 1 of only +0.2% GDP growth, the three subsequent quarters of 2016 came in at +0.6%, +0.5% and +0.7% to produce an annual growth for 2016 overall, compared to 2015, of no less than 1.8%, which was very nearly the fastest rate of growth of any of the G7 countries. Needless to say, this meant that the MPC did not cut Bank Rate again after August but, since then, inflation has risen rapidly due to the effects of the sharp devaluation of sterling after the referendum.

## 3.0 Overall Treasury Position as at 31 March 2017

- 3.1 At the beginning and the end of 2016/17 the Council's treasury (excluding borrowing by private finance initiatives (PFI) and finance leases) position is outlined in Table 1.

**Table 1 - Overall Treasury Position as at 31 March 2017**

	31 March 2016 Principal £'000	Rate/ Return	Average Life Years	31 March 2017 Principal £'000	Rate/ Return	Average Life Years
General Fund (GF) debt	9,179	3.26%	13.8	11,629	3.14%	14.2
Housing Revenue Account (HRA) debt	20,041	4.03%	9.7	20,040	4.03%	8.9
<b>Total debt</b>	<b>29,220</b>	<b>3.78%</b>	<b>11.0</b>	<b>31,669</b>	<b>3.71%</b>	<b>10.8</b>
<b>GF CFR</b>	27,067			26,706		
<b>HRA CFR</b>	20,241			20,377		
<b>Total CFR</b>	<b>47,308</b>			<b>47,083</b>		
<b>Over / (under) borrowing</b>	<b>(18,088)</b>			<b>(15,414)</b>		
<b>Total investments</b>	<b>28,612</b>	<b>0.55%</b>		<b>37,988</b>	<b>0.49%</b>	
<b>Net debt / (investment)</b>	<b>608</b>			<b>(6,319)</b>		

#### 4.0 The Strategy for 2016/17

- 4.1 The expectation for interest rates within the treasury management strategy for 2016/17 anticipated low but rising Bank Rate, (starting in quarter 2 of 2016), and gradual rises in medium and longer term fixed borrowing rates during 2016/17. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.
- 4.2 In this scenario, the treasury strategy was to postpone borrowing to avoid the cost of holding higher levels of investments and to reduce counterparty risk.
- 4.3 During 2016/17 there was major volatility in PWLB rates with rates falling during quarters 1 and 2 to reach historically very low levels in July and August, before rising significantly during quarter 3, and then partially easing back towards the end of the year.
- 4.4 **Change in strategy during the year** – the strategy adopted in the original Treasury Management Strategy Report for 2016/17 approved by the Council on 04/02/16 was not revised during 2016/17.

#### 5.0 The Borrowing Requirement and Debt

- 5.1 The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR) is shown in Table 2.

**Table 2 - Council's Capital Financing Requirement**

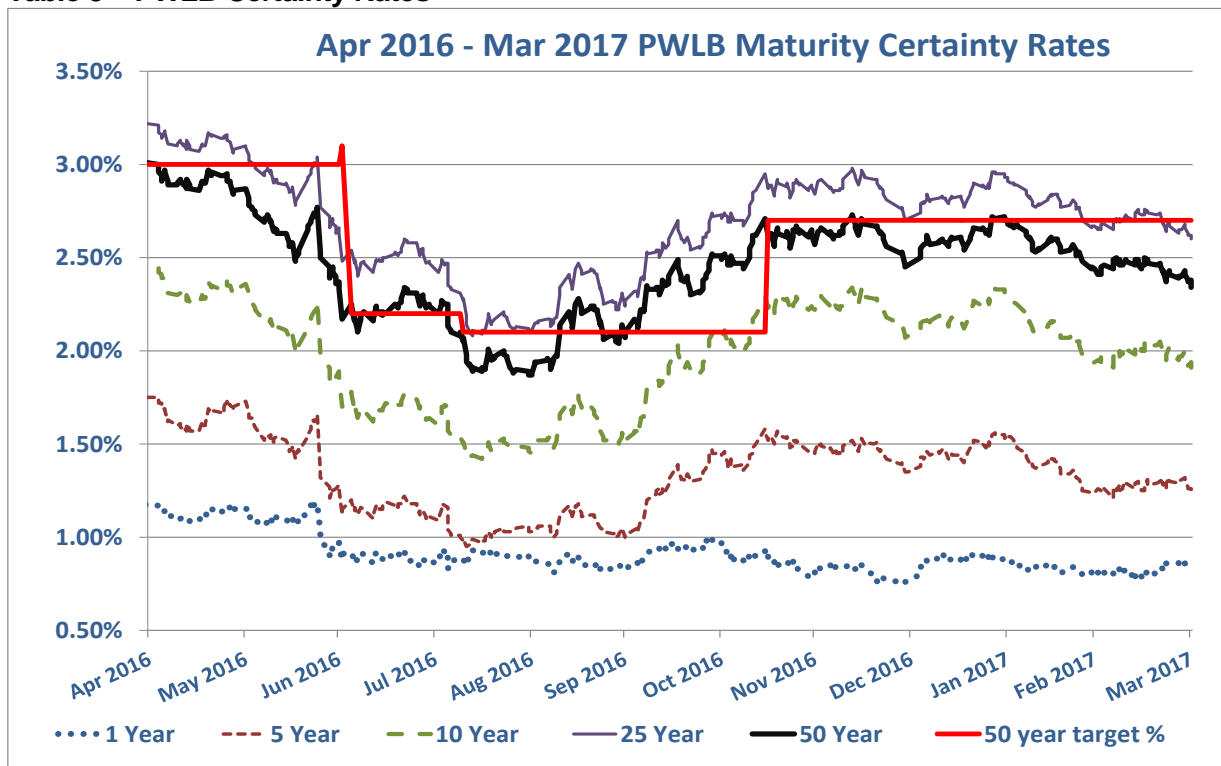
	31 March 2016 Actual £'000	31 March 2017 Budget £'000	31 March 2017 Actual £'000
CFR General Fund (GF)	27,067	29,189	26,706
CFR Housing Revenue Account (HRA)	20,241	27,477	20,377
Total CFR	47,308	56,666	47,083

The 2016/17 HRA capital expenditure budget included £14.5m subsequently re-profiled to 2017/18 in the Budget and Medium Term Financial Strategy 2017/21. This re-profiled amount was due to increase the HRA Capital Financing Requirement by £6.7m.

#### 6.0 Borrowing Rates in 2016/17

- 6.1 **Public Works Loan Board (PWLB) certainty maturity borrowing rates** - the graph in Table 3 shows how PWLB certainty rates have fallen to historically very low levels during the year.

**Table 3 – PWLB Certainty Rates**



**7.0 Borrowing Outturn for 2016/17**

7.1 **Borrowing** – Table 4 outlines the General Fund loans drawn from the PWLB to fund net unfinanced capital expenditure and any naturally maturing debt:

**Table 4 –General Fund Loans from PWLB in 2016/17**

Principal £000	Type	Interest Rate	Maturity	GF Average Interest Rate for 2016/17
2,000	Fixed interest rate - Maturity	3.09%	18/10/2038	3.14%
1,000	Fixed interest rate - EIP	1.28%	20/06/2023	3.14%

This compares with a budget assumption of borrowing at an interest rate of 5% for the £2m loan and 4% for the £1m loan.

7.2 **Rescheduling** – No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

7.3 **Repayments** – The Council repaid £550k of maturing debt using investment balances. Details of these are outlined in Table 5.

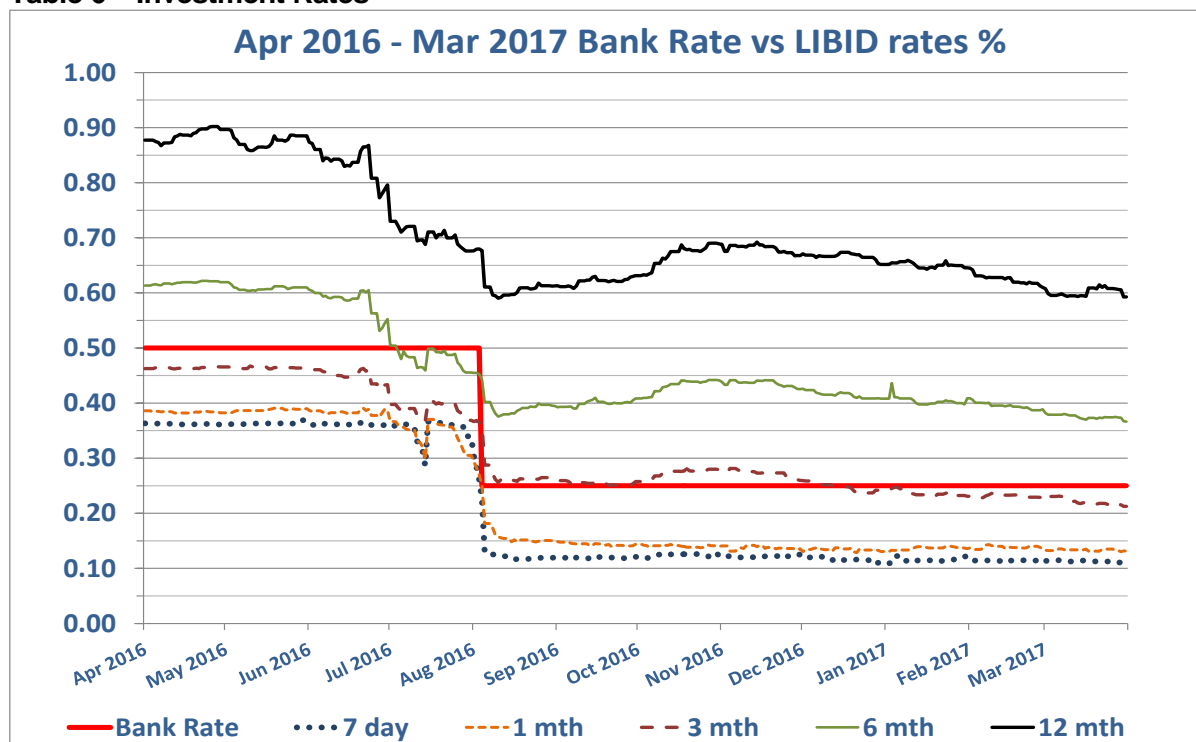
**Table 5 – PWLB Maturing Debt Paid in 2016/17**

Lender	Principal £'000	Interest Rate	Repayment Date
PWLB	43	3.08%	23/04/16
PWLB	50	2.48%	27/05/16
PWLB	146	1.97%	27/05/16
PWLB	43	3.08%	23/10/16
PWLB	50	2.48%	27/11/16
PWLB	146	1.97%	27/11/16
PWLB	72	1.28%	20/12/16
<b>Total</b>	<b>550</b>		

7.4 **Summary of debt transactions** – The above changes in the debt portfolio resulted in a decrease in the average interest rate of 0.07%, representing an interest saving of £22k on the weighted average of the 2016/17 debt principal.

#### 8.0 Investment Rates in 2016/17

**Table 6 – Investment Rates**



8.1 After the EU referendum, the Bank of England Base Rate was cut from 0.5% to 0.25% on 4 August and remained at that level for the rest of the year. Market expectations as to the timing of the start of monetary tightening started the year at quarter 3, 2018, but then moved back to around the end of 2019 in early August before finishing the year back at

quarter 3, 2018. Deposit rates continued into the start of 2016/17 at previous depressed levels but then fell during the first two quarters and fell even further after the 4 August MPC meeting resulted in a large tranche of cheap financing being made available to the banking sector by the Bank of England. Rates made a weak recovery towards the end of 2016 but then fell to fresh lows in March 2017.

## **9.0 Investment Outturn for 2016/17**

9.1 **Investment Policy** – the Council's investment policy is governed by Department for Communities and Local Government (CLG) guidance, which has been implemented in the annual investment strategy approved by the Council on 4 February 2016. This policy sets out the approach for choosing investment 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.).

9.2 The investment activity during the year conformed to the approved strategy, apart from exceeding the £0.5m bank overdraft benchmark for one day only. This was a technical breach and the Council had no liquidity difficulties during the year.

9.3 **Investments held by the Council** - the Council maintained an average balance of £43.47m of internally managed funds. The internally managed funds earned an average rate of return of 0.49%. The comparable performance indicator is the average 7-day London Interbank Bid Rate (LIBID) rate, which was 0.20%. This compares with a budget assumption of £20m investment balances earning an average rate of 0.90%.

9.4 **Investments held by fund managers** – the Council does not use external fund managers.

## **10.0 Investment risk benchmarking**

10.1 The following investment benchmarks were set in the Council's 2016/17 annual treasury strategy:

10.2 **Security** - The Council's maximum security risk benchmark for the current portfolio, when compared to historic default tables, is:

- 0.05% historic risk of default when compared to the whole portfolio.

10.3 **Liquidity** – in respect of this area the Council seeks to maintain:

- Bank overdraft - £0.5m
- Liquid short term deposits of at least £10m available with a week's notice.
- Weighted average life benchmark is expected to be 0.5 years, with a maximum of 1.0 year.

10.4 **Yield** - local measures of yield benchmarks are:

- Investments – internal returns above the 7 day LIBID rate

10.5 The Council kept to the above benchmarks during 2016/17 apart from exceeding the bank overdraft benchmark as referred to in section 9.2 above.

## 11.0 Options

11.1 The recommended option (to ensure regulatory compliance as set out in section 1 of this report) is that Council:

- Notes the actual 2016/17 prudential and treasury indicators in this report.
- Approves the Annual Treasury Management report for 2016/17.

11.2 Alternatively, Council may decide not to do this and provide reason(s) why.

## 12.0 Disclaimer

12.1 This report is a technical document focussing on public sector investments and borrowings and, as such, readers should not use the information contained within the report to inform personal investment or borrowing decisions. Neither Thanet District Council nor any of its officers or employees makes any representation or warranty, express or implied, as to the accuracy or completeness of the information contained herein (such information being subject to change without notice) and shall not be in any way responsible or liable for the contents hereof and no reliance should be placed on the accuracy, fairness or completeness of the information contained in this document. Any opinions, forecasts or estimates herein constitute a judgement and there can be no assurance that they will be consistent with future results or events. No person accepts any liability whatsoever for any loss howsoever arising from any use of this document or its contents or otherwise in connection therewith.

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Reporting to:	Madeline Homer, Chief Executive

## Annex List

Annex 1	Prudential and Treasury Indicators
Annex 2	Report Guidance
Annex 3	Abbreviations and Definitions

## Corporate Consultation Undertaken

Finance	Ramesh Prashar, Head of Financial Services
Legal	Tim Howes, Director of Corporate Governance & Monitoring Officer