TO:	Audit Committee
FROM:	Executive Director Resources and Transformation
DATE:	13th January 2015

TITLE OF BRIEFING PAPER: Treasury Management Report – Sep to Nov 2014

1. PURPOSE

1.1 To allow scrutiny of the Treasury Management function.

2. RECOMMENDATIONS

2.1 Members are recommended to note the position with regard to Treasury Management for the period September to November 2014 AND the key issues to be addressed in the forthcoming Treasury Management Strategy Proposals for 2015-16.

3. BACKGROUND

3.1 The Council has previously adopted CIPFA's latest *Code of Practice on Treasury Management in the Public Services* and associated Guidance Notes. The Treasury Management Strategy for 2013/14 and the strategy for 2014/15, approved at Finance Council on 3rd March 2014, comply with both the CIPFA Code and with current CLG guidance on Investments (issued in March 2010). The CIPFA Code, Investment Guidance issued by the Department for Communities and Local Government (CLG) and Audit & Assurance reviews of Treasury Management activities all recommend an enhanced role for elected members in scrutinising the Treasury Management function of the Council.

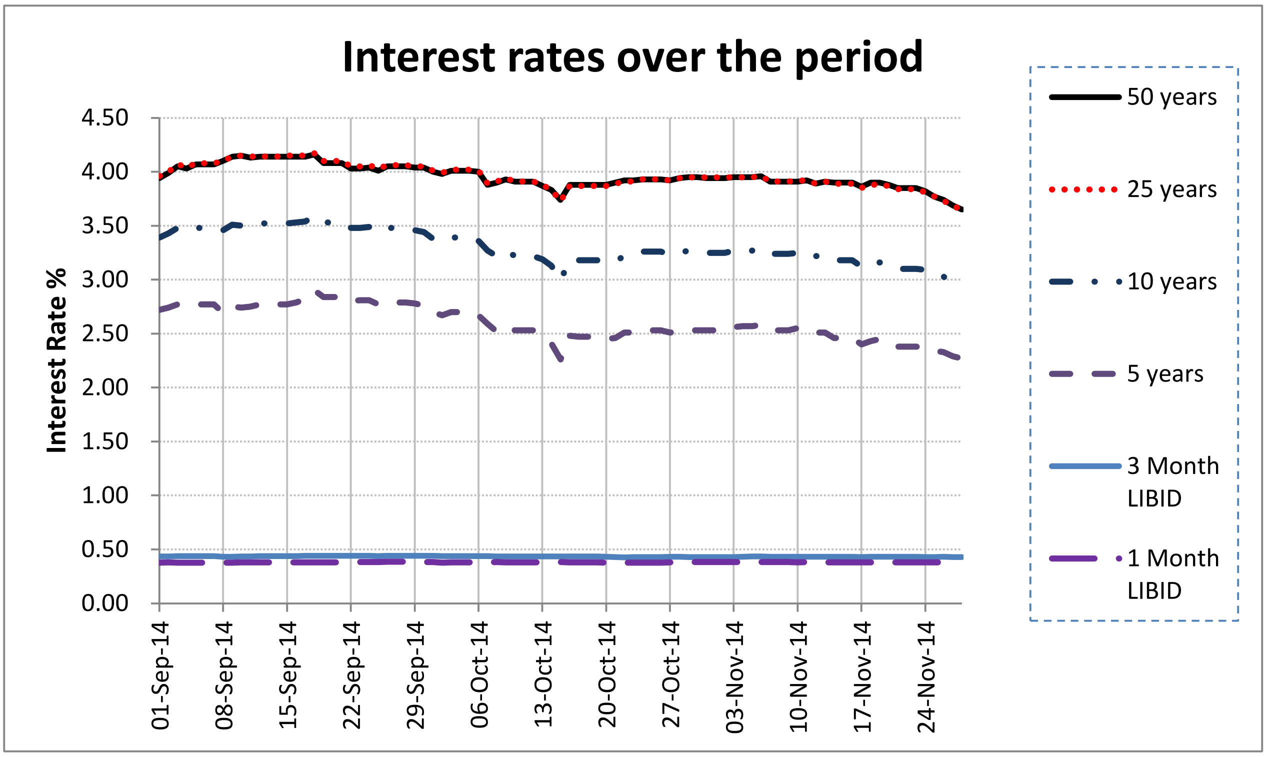
3.2 This report summarises the interest rate environment for the three months, borrowing and lending transactions undertaken and the Council's overall debt position. It also reports on the position against the Prudential Indicators established by the Council.

4. RATIONALE

4.1 Audit Committee is responsible for scrutinising the Treasury Management function.

5. KEY ISSUES

5.1 <u>Interest rates</u>



5.1.1 The Bank of England Bank Rate held at 0.5% over the period. It has been at this level since March 2009. LIBID and PWLB rates are set out above

5.1.2 The interest rates for durations of less than a year are represented by LIBID (London Interbank Bid Rate), a standard measure of current market rates. In previous years this report had used the LIBOR (Offer Rate) but it is now considered that the LIBID (around 0.125% lower) represents a better benchmark for investment returns.

5.1.3 The rates actually available to the authority for investing funds in the limited range of approved counterparties remained low, mainly ranging from 0.25% to 0.50%, with returns on instant access bank deposits falling, while returns on money market funds and fixed term deposits moved up a little.

5.1.4 In order to show the potential costs of borrowing to fund the Council's capital programme, the rates shown for 5 years and beyond are PWLB Lending Rates for straightforward "Maturity" Loans (interest payable for fixed rate borrowing by councils over fixed periods). These are largely driven by the demand from investors for Government borrowing ("gilts"). These rates fell, particularly over the latter part of the period, as relative interest rates and continuing economic weakness in the Eurozone enhanced the "safe haven" status of UK government bonds.

5.2 Borrowing and lending movements

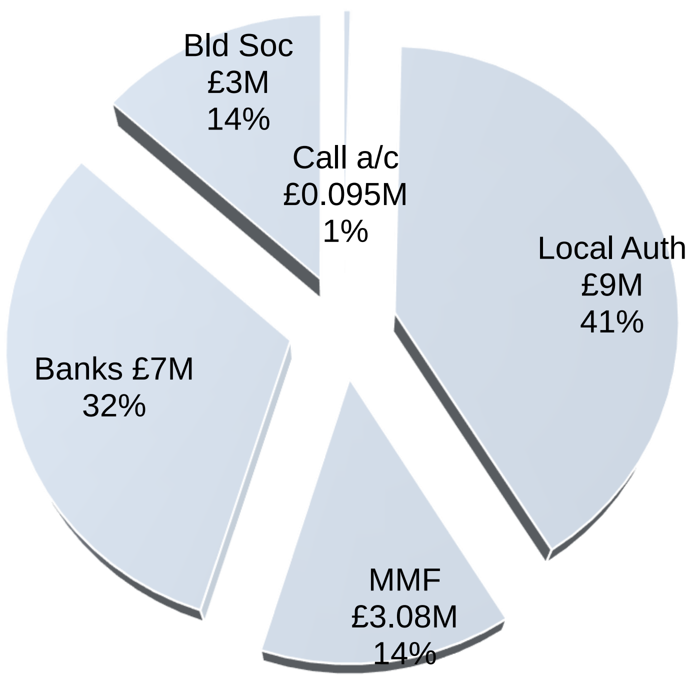
5.2.1 No borrowing was taken in 2014/15, until the end of September. A series of short-term loans has been taken (scheduled at 5.4.1, below) to help meet immediate cash flow requirements, as this represented better value than taking on new longer term debt. Though short term borrowing is significantly cheaper than long term borrowing, thereby yielding savings against originally estimated borrowing costs, if there are any signs of significant increases in PWLB rates, the long term impact of delays to taking up long term borrowing will also need to be considered.

5.2.2 We are under-borrowed against our Capital Financing Requirement, effectively using "internal borrowing" from available cash balances to cover outstanding capital borrowing requirements. A positive side-effect of this is a reduction in the risks of funds invested being lost and of interest being foregone through the cost of borrowing being higher than the return to be made from investments.

5.2.3 New investments were largely of a short duration, mainly in either "call accounts" or "money market funds" (with daily access to funds). The interest earned on these was in the range 0.25% to 0.42%. The Debt Management Office, an arm of the Government, can also be used to place funds at 0.25% for limited periods when there are no other options available within our lending limits. In addition, the following loans were made during the quarter:

Start Date	End Date	Counterparty	Amount £	Rate %
22-Sep-14	23-Mar-15	Cornwall County Council	£2,000,000	0.400
28-Aug-14	03-Mar-15	Aberdeen County Council	£3,000,000	0.490
29-Aug-14	29-Sep-14	Thurrock Borough Council	£1,000,000	0.300
29-Aug-14	28-Nov-14	Leeds Building Society	£1,000,000	0.400
29-Aug-14	28-Nov-14	Coventry Building Society	£1,000,000	0.450
23-Sep-14	23-Dec-14	Santander UK	£3,000,000	0.550
29-Sep-14	19-Dec-14	Nationwide Building Society	£3,000,000	0.480
28-Nov-14	13-Jan-15	Plymouth City Council	£2,000,000	0.430

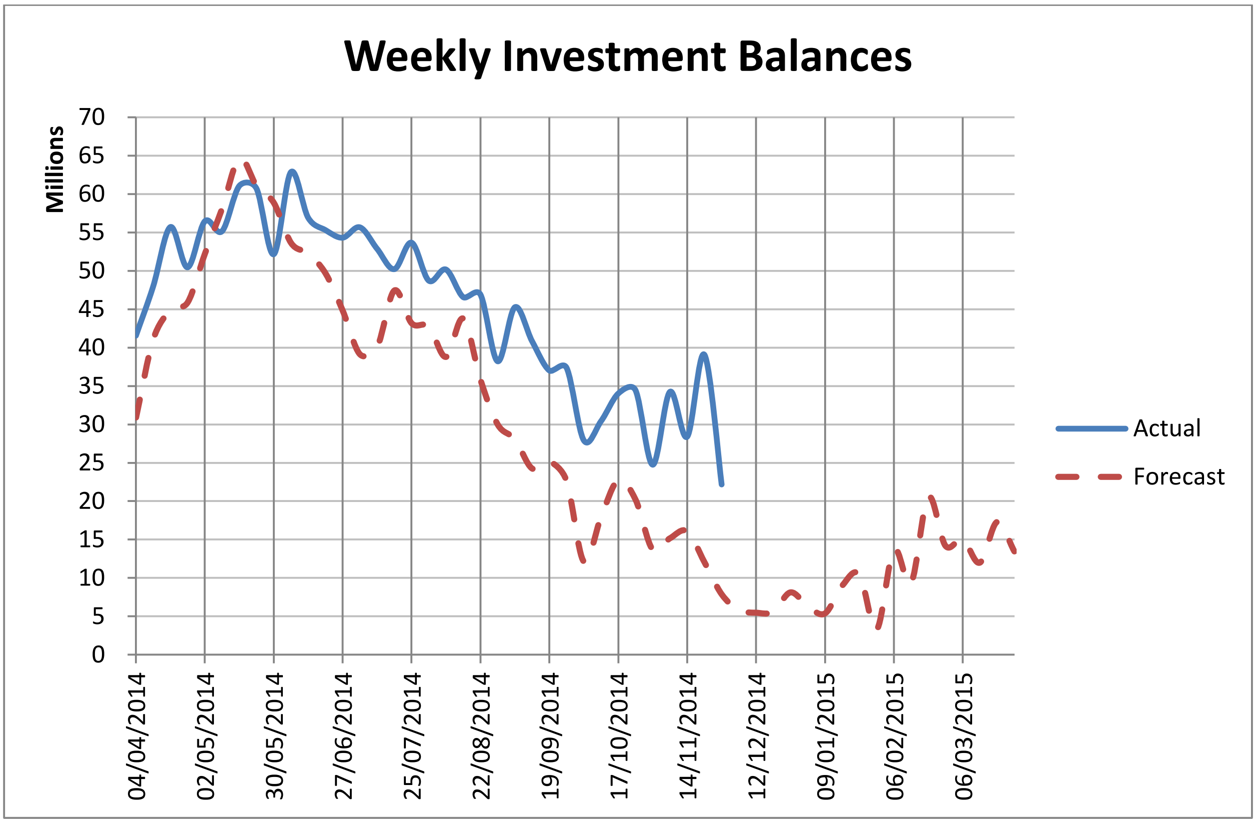
The chart below shows a breakdown of the £22.2M invested at the end of November 2014.



5.3 Amounts available for investment

5.3.1 For 2014/15 Government grant receipts were again front-loaded, which has resulted in large cash balances in the first part of the year - up to a maximum of £63M in May – with balances then falling away over the summer.

5.3.2 Balances were expected to continue to fall steadily before increasing in the final quarter (when the remainder of the main grant funding is received) but recently taken short term loans have helped maintain liquidity at higher levels.



5.4 The Council's debt

5.4.1 The Council took five temporary (or short term) loans in the period 1-Sep to 30-Nov (see breakdown below).

Start Date	End Date	Counterparty	Amount £	Rate %
30/09/2014	01/10/2014	Rhonnda Cynon Taff	2,185,000	0.28
08/10/2014	08/01/2015	London Borough of Camden	5,000,000	0.47
19/11/2014	28/01/2015	Worcestershire County Council	2,000,000	0.32
05/11/2014	05/02/2015	Caerphilly County Borough Council	5,000,000	0.30
05/11/2014	28/11/2014	Bridgend County Borough Council	3,000,000	0.30

5.4.2 The key elements of our long term borrowing are:

a) An unchanged £23.5M borrowed from the money markets, largely in the form of "LOBO" debt, which is borrowed at competitive interest rates at the time of borrowing, but can carry some risks in terms of interest rate increases or early redemption. The overall average rate paid on this debt is 5.2%.

b) £117.5M borrowed from the PWLB at a range of fixed rates, at an overall average rate of around 4.4%. At the end of September we made EIP principal repayments of c. £0.8M and repaid a £1.1M maturity loan.

c) Approximately £17.7M debt still managed by Lancashire County Council following Local Government Reorganisation, which is repaid in quarterly instalments across the year – in 2013/14, the average rate was around 2.5%, and the latest projected rate for the current year is c. 2.75%.

d) Debt recognised on the balance sheet as a result of accounting adjustments in respect of bringing into use the new BSF School buildings, financed through PFI arrangements. These accounting adjustments are made to ensure that the Council's effective control over and use of these assets are shown "on balance sheet", with corresponding adjustments to the debt. The accounting changes do not add to the costs faced by the Council Tax payer, which are already paid for through the payments made to the PFI contractor (which are, in turn, largely offset by PFI grant funding from the Government).

Analysis of debt outstanding					
		Start of September 2014		End of November 2014	
		£' 000	£ ' 000	£' 000	£ ' 000
TEMPORARY DEBT					
	Less than 3 months	0		12,000	
	Greater than 3 months	0		0	
			0		12,000
LONGER TERM DEBT					
	Bonds	23,503		23,503	
	Mortgages	17		17	
	PWLB	119,403		117,475	
	Stock & Annuities	404		404	
			143,327		141,399
Lancs County Council transferred debt			17,894		17,713
Recognition of Debt re PFI Arrangements			72,408		72,035
TOTAL DEBT			233,629		243,147
Less: Temporary Lending			41,864		22,173
			191,765		220,974

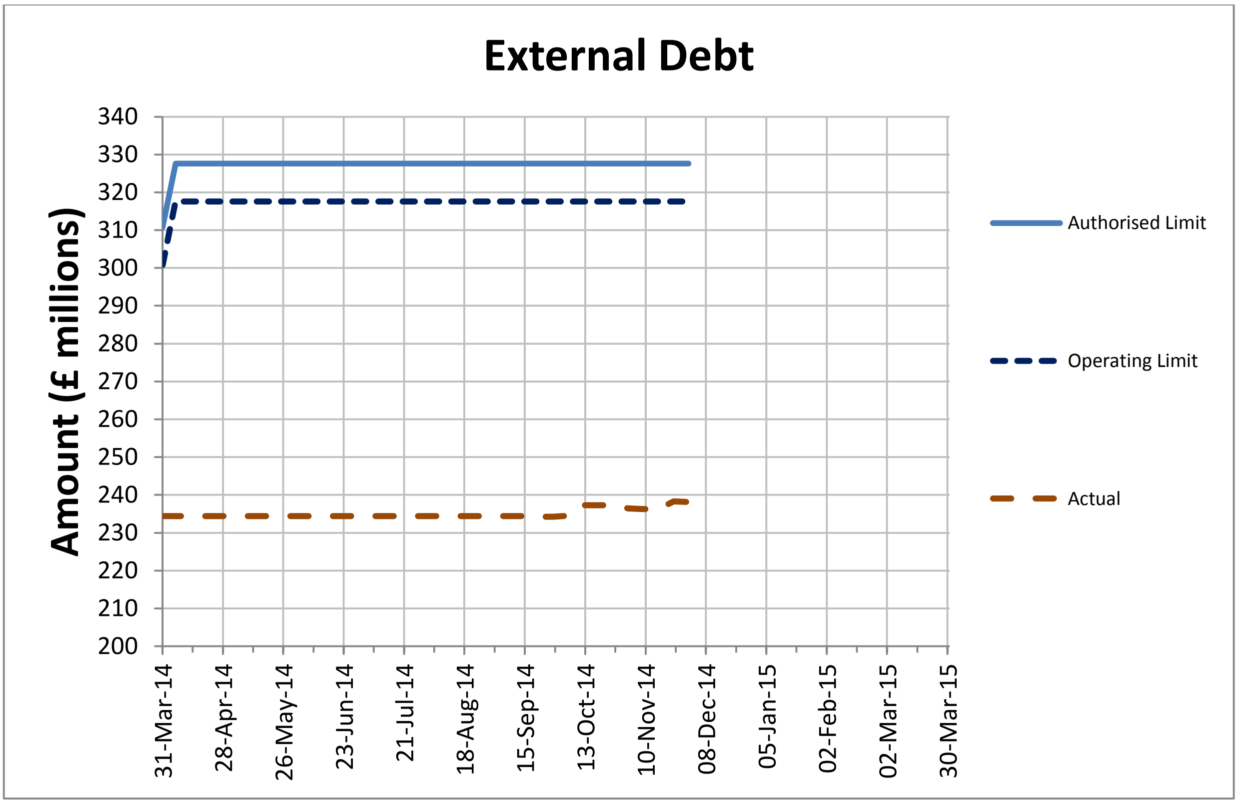
The changes across the period were in respect of the usual LCC debt repayments, short term borrowing and PWLB payments already mentioned and a significant fall in cash held / temporary lendings, giving an overall increase in the net debt.

5.5 Performance against prudential and treasury indicators

5.5.1 Prudential Indicators are established mainly to allow members to be informed of the impact of capital investment decisions and to establish that the proposals are affordable, prudent and sustainable. In addressing the debt taken on by the Council, the indicators also deal, therefore, with treasury issues, in particular the absolute level of debt being taken on (through the Authorised and Operational Borrowing Limits).

5.5.2 Appendix 1 shows the current position against the Prudential Indicators set by the Council for the current year. None of the key Indicators have been breached.

5.5.3 Our borrowing position was at £238.1M against our Authorised and Operational Borrowing Limits (£327.6 million and £317.6 million respectively) – this is the most significant Prudential Indicator.

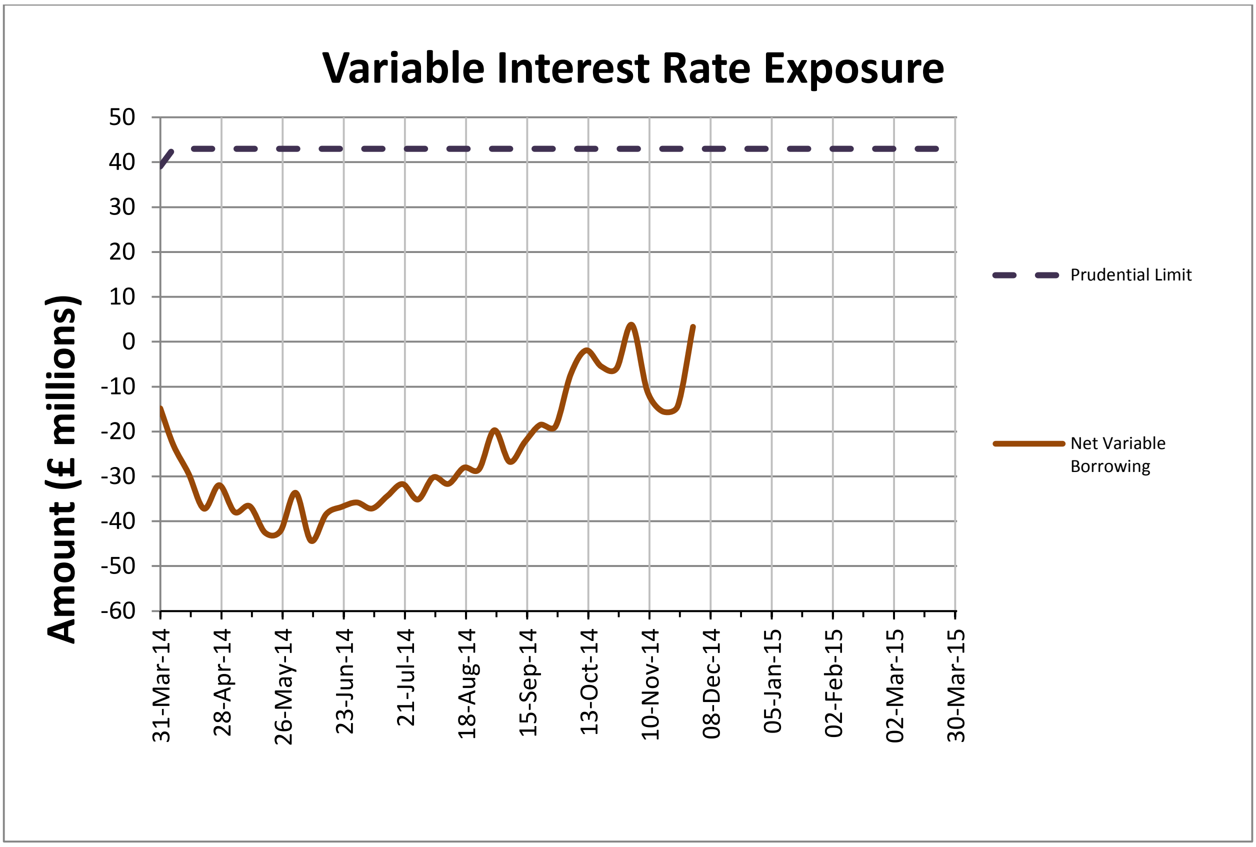


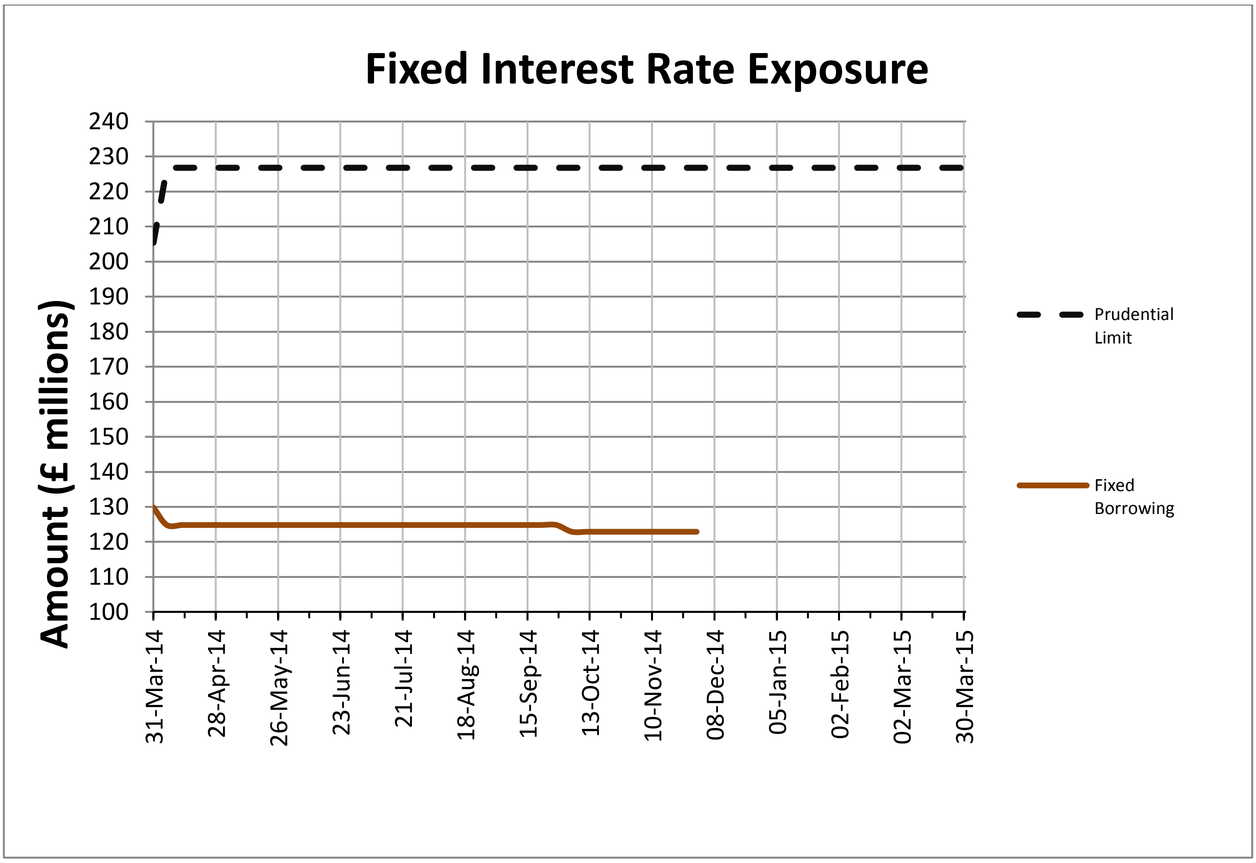
5.5.4 The above "actual borrowing" includes the impact on the balance sheet of the recognition of assets brought into use that have been financed through PFI. The accounting adjustments are designed to show our effective long term control over the assets concerned, and the parallel "indebtedness" arising from financing the cost of them, but do not add to the "bottom line" met by the Council Tax payer.

5.6 <u>Interest risk exposures</u>

5.6.1 Our Variable Interest Rate Exposure ended the period at around £3.8M, and remained within the limit set at +£43M for 2014/15 across the period. This indicator exists to ensure that the Council does not become over-exposed to changes in interest rates impacting adversely on its revenue budget. It tracks together the variable parts of the debt portfolio and the investment portfolio.

5.6.2 Our Fixed Interest Rate Exposure is £122.9M, against a Limit of £226.8M for 2014/15. This indicator is effectively the mirror image of the previous indicator, tracking the Council's position in terms of how much of the debt will not vary as interest rates move. The historically low interest rates prevailing over recent years have led the Council to hold most of its debt in this way.





5.7 Treasury Management Strategy for 2015-16

5.7.1 The Council will approve a new Treasury Management Strategy for 2015-16 when approving the budget proposals at Finance Council in early March. At the same time the Council's proposed Prudential Indicators for 2015-16 are set (which heavily depend on capital programme forecasts) and policy proposals for determination of Minimum Revenue Provision (MRP) for repayment of debt are set. The key issues and potential changes to the Strategy are summarised below.

5.7.2 The Strategy report will cover

(a) the control framework and financial/economic contexts underpinning the establishment of the Strategy,

(b) Borrowing Strategy - likely levels of Council Debt and how it is proposed to manage that debt. Given the significant cuts to local government funding, the strategy will address the key issue of affordability without compromising the longer-term stability of the debt portfolio. The continued use of internal resources and short-term borrowing – as against taking out extensive new long-term debt – will be noted, while recognising that this will be monitored regularly against the potential for incurring additional long-term costs by deferring borrowing into future years (at higher rates).

(c) Investment Strategy - how the risks associated with investment are to be managed. Changes to the regulatory and risk regimes around banking mean that public authorities and financial organisations (including pension funds) will face increased risks as the only senior creditors likely to incur losses in a failing bank after July 2015. In this context, the framework for setting investment limits will need to be amended, and consideration given to alternative investment options (both more secure and in some cases higher yielding), to increase diversification, and obtain a better trade-off between risk and return. There could therefore be a material change in strategy over the coming year, but current prudent priorities, emphasising Security and Liquidity over Yield, will be maintained.

The overall priority of the Treasury Strategy will be to take any prudent options available to reduce the overall cost of debt to the Council.

5.7.3 The Council's MRP policy - for setting the amount to be charged to revenue for debt repayment each year – will be reviewed and if there are prudent opportunities to make savings in this area they will be considered and may be reflected in the proposals.

6. POLICY IMPLICATIONS

6.1 The policy implications from this report are contained within the Council's overall Budget Strategy.

7. FINANCIAL IMPLICATIONS

7.1 The financial implications arising from Treasury Management activities are reflected in the Council's standard budget monitoring framework.

8. LEGAL IMPLICATIONS

8.1 The report is in accordance with the CIPFA code and therefore is in accordance with the Financial Procedure Rules under the Council's Constitution.

9. RESOURCE IMPLICATIONS

9.1 None

10. EQUALITY IMPLICATIONS

10.1 The decisions to be taken do not change policy and do not require any further consideration in respect of equality issues.

11. CONSULTATIONS

11.1 None

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DATE:	19th December 2014
BACKGROUND PAPERS:	CIPFA Code of Practice and Guidance Notes on Treasury Management in the Public Services (2011)