

# Overview and Scrutiny Committee

12 July 2016



<b>Title</b>	Treasury Management Annual Report 2015-16		
<b>Purpose of the report</b>	To note		
<b>Report Author</b>	Ryan Maslen		
<b>Cabinet Member</b>	Councillor Howard Williams	<b>Confidential</b>	No
<b>Corporate Priority</b>	Value for money Council		
<b>Cabinet Values</b>	Self-Reliance and Accountability		
<b>Recommendations</b>	<b>The Committee is asked to note the contents of this report.</b>		

## 1. Key issues

### Background

- 1.1 The Chartered Institute of Public Finance and Accountancy's Treasury Management Code (CIPFA's TM Code) requires that authorities report on the performance of the treasury management function at least twice a year (mid-year and at year end).
- 1.2 The Council's Treasury Management Strategy for 2015/16 was fully approved by Cabinet in January 2015 and Council in February 2015.
- 1.3 The Authority has invested and borrowed substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. This report covers treasury activity and the associated monitoring and control of risk.

### Compliance with Treasury Limits

- 1.4 During the financial year the Council operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Policy Statement and annual Treasury Strategy Statement. The outturn Prudential Indicators for 2015/16 are shown in Appendix A.

### Strategy for the Year 2015/16

- 1.5 The Guidance on Local Government Investments in England gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles.
- 1.6 The Bank of England base rate remains at 0.5% and with an increase not expected by our treasury advisors Arlingclose until quarter two of 2018, the Council continues to regularly review its treasury strategy to support the revenue budget process.

- 1.7 Investments are managed in house and the Council has continued to place part of its core investment portfolio in pooled investment funds to achieve higher returns. Our total investment in such arrangements increased to just under £9.5m in 2015/16, over a range of equity, property and corporate bond funds. These continue to perform exceptionally well compared to the current returns available for cash and fixed term deposits, generating an average return of just under 5%.
- 1.8 This performance fully supports the decision taken a number of years ago to widen the investment strategy. In addition to the annual return generated, there are also significant capital gains of £0.7m on the initial investments made, and a breakdown of these is shown in paragraph 2.11 below.
- 1.9 Although money can be redeemed from the pooled funds at short notice, the Authority's intention is to hold them for the medium-term. Their performance and suitability in meeting the Authority's investment objectives are monitored regularly and discussed with Arlingclose.
- 1.10 The Council's remaining funds are managed from an overall cash flow perspective, although maturities are extended wherever possible to improve returns. A number of fixed term deposits have been made throughout the year, along with deposits in instant access accounts and money market funds. The Council continues to look to identify additional new investment options with the aim of increasing the return received and achieving greater diversification. The Council's cashflow requirements and income stream profiles are relatively predictable and this has enabled use of notice accounts during 2015/16. These are offered by a number of banks and provide a significant increase on the rates available on traditional instant access accounts, therefore maximising the returns to the Council.

## **2. Options analysis and proposal**

### **Performance in 2015/16**

- 2.1 Borrowing activity is extremely limited at the present time for the Council. There was a requirement to borrow a small sum in March 2016 to meet a short term unexpected cash flow need. This was borrowed from two other Local Authorities, with one amount being repaid in June 2016 and the other in August 2016. An element of flexibility to potential borrowing will be imperative going forward to support the Council in its period of transformation as part of the Towards a Sustainable Future agenda. It is anticipated that any significant capital acquisitions in the near future will be funded from borrowing. The Council is regularly liaising with its advisors on the right borrowing strategy to pursue.
- 2.2 The Council manages its investments in-house and invests with the most highly rated counterparties. During the year all investments were made in full compliance with the Council's treasury management policies and practices and in consultation with Arlingclose.
- 2.3 As at 31<sup>st</sup> March 2016 the net investment portfolio held by the Council was £18.24m. Full details of all investments held are shown in Appendix B.
- 2.4 The Council had originally estimated net investment income of £635k to be credited to the General Fund in 2015/16. This was a prudent estimate based on historical performance (interest income was £535k in 2014/15) and this

also took into consideration the significant capital receipt that the Council anticipated receiving during the financial year, which would be reinvested.

2.5 The actual interest outturn for the year was £599,649 made up as follows:

<b>Investment Income</b>	<b>Actual £</b>	<b>Budget £</b>
Temporary Investments & Cash Deposits	113,153	100,000
Pooled Equity & Bond Funds	486,496	535,000
<b>Total Investment Income</b>	<b>599,649</b>	<b>635,000</b>

2.6 The outturn position reflects the delay in the Council receiving the capital receipts that were expected within 2015/16. Every effort has been made to maximise the return achieved and minimise the shortfall in meeting the budget expectation. In comparison to 2014/15, additional investment income of £65k (a 12% increase) has been generated, which against the background of continuing low interest rates is a significant achievement.

#### **Investment Performance Monitoring**

2.7 Regular quarterly meetings of officers and the Portfolio holder are held with Arlingclose and in-house performance is monitored monthly. The Council is heavily dependent on investment returns to support the General Fund and the stability of those returns is an important part of our ongoing financial objectives.

2.8 Creditworthiness is also monitored regularly. The Council uses Arlingclose's suggested criteria to assist in the selection of suitable investment counterparties. This is based on credit ratings, including sovereign ratings, provided by the three main ratings agencies and supplemented by additional market data including rating outlooks, credit default swaps, bank equity prices etc. to assist the Council in making more informed decisions about which counterparties to invest with. However, the final selection decision always rests with the Council.

2.9 The end of bank bail-outs, the introduction of bail-ins, and the preference being given to large numbers of depositors other than local authorities means that the risks of making unsecured deposits continues to be elevated relative to other investment options. The Authority therefore increasingly favoured secured investment options or diversified alternatives such as non-bank investments and pooled funds over unsecured bank and building society deposits.

#### **Conclusions for 2015/16 and Prospects for 2016/17**

2.10 Market interest rates remain at historically low levels and Arlingclose believe these are unlikely to increase until quarter 2 of 2018. The return on investments achieved in 2015/16 has therefore been very good considering the external economic conditions the Council has to operate within. The major contributing factor to this has been the Pooled Investment Funds.

- 2.11 As at 31st March 2016 the Council had £9.49m invested in these longer term arrangements. In addition to this, as at 31<sup>st</sup> March 2016 there was a capital gain of £0.7m on these funds and this is detailed in the table below:

<b>Pooled Fund Asset Class</b>	<b>Original Investment</b>	<b>Market Value at 31/3/16</b>
Equity Funds	£3.8m	£3.93m
Corporate Bond Funds	£3.19m	£3.23m
Property Funds	£2.5m	£3.04m
<b>Total Investment</b>	<b>£9.49m</b>	<b>£10.2m</b>

- 2.12 Capital gains can vary on a daily basis and cannot be realised unless the investments are sold. Past performance is also no guide to the future but no treasury management activity is without risk so a balanced portfolio containing a good mix of asset classes can help to mitigate and manage risk effectively.
- 2.13 The Council's portfolio will continue to be kept under constant review in consultation with our treasury advisors to optimise investment performance whilst keeping risk to a minimum. The Council is proactive in its treasury management strategy so that it can act quickly when market conditions change.
- 2.14 With the significant capital receipts that are due to the Council in the near future, planning work has already commenced in conjunction with the portfolio holder and Arlingclose to establish the most effective way to reinvest these funds. The pooled fund investments are a natural starting point for these discussions and with the need to maintain a balanced portfolio a number of new fund options are currently being appraised.
- 2.15 With diversification of the overall portfolio also in mind, the Council has recently made a fixed term loan for a period of five years at a rate of 3.6% to Network Housing Group. Full due diligence was completed before this arrangement was entered into to ensure suitability, and the Council may look to make similar loans to other Housing Associations in the future if an appropriate opportunity becomes available.
- 2.16 The Council will also be working closely with Knowle Green Estates Ltd in the future, offering finance to the new entity at commercial rates. This will provide the Council with an additional fixed income stream and further diversification of the portfolio.

### **3. Financial implications**

- 3.1 This report is a review of past investment performance and the financial implications are as set out in this report. The ability of the Council to generate maximum net investment returns with minimal risk provides significant resources for funding the Council's services.

### **4. Other considerations**

- 4.1 There are none.

### **5. Timetable for implementation**

5.1 Treasury management is an ongoing activity and normally there is no specific timetable for implementation.

**Background papers:** None

**Appendices:** A & B

**PRUDENTIAL INDICATORS  
ACTUALS 2015/16**

<b>Capital Expenditure Prudential Indicators</b>	<b>2014/15 Actual Outturn</b>	<b>2015/16 Original Estimate</b>	<b>2015/16 Actual Outturn</b>
Prudential Indicator	£'000	£'000	£'000
Capital Expenditure	1,905	10,955	1,551
Ratio Financing Costs to Net Revenue Stream	(4.11)	(4.65)	(4.38)
Net Longer-term Borrowing	£0	£0	£0
In year Capital Financing Requirement	£0	£0	£0
Capital Financing Requirement as at 31 <sup>st</sup> March	£0	£0	£0

<b>Treasury Management Prudential Indicators</b>	<b>2014/15 Actual</b>	<b>2015/16 Original Estimate</b>	<b>2015/16 Actual Outturn</b>
Prudential Indicator	£'000	£'000	£'000
Authorised Limit for external debt	12,000	12,000	12,000
Operational Boundary for external debt	10,000	10,000	10,000
Gross Debt to Capital Finance Requirement	£0	£0	£0
Upper limit for fixed rate exposure	100%	100%	100%
Upper limit on variable rate exposure	100%	100%	100%
Upper limit principal invested for over 364 days	15,000	15,000	15,000

<b>Maturity structure of fixed rate borrowing</b>	<b>Upper limit</b>	<b>Lower limit</b>
Under 12 months	£12,000,000	£Nil
12 months but within 24 months	£Nil	£Nil
24 months but within 5 years	£Nil	£Nil
5 years but within 10 years	£Nil	£Nil
10 years and above	£Nil	£Nil

<b>Actual External Debt as at 31/3/16</b>	£4.03m (all short term borrowings)
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**Details of Investments Held as at 31<sup>st</sup> March 2016**

<b>Investment Type</b>	<b>Amount £m</b>	<b>Interest Rate %</b>	<b>Start Date</b>	<b>Maturity Date</b>
<u>Pooled Investment Funds</u>				
Charteris Elite Equity Income	0.8	3.39%	May 2012	N/A
Schroeders UK Corporate Bond	1.5	5.07%	May 2012	N/A
M&G Optimal Income Sterling	1.69	2.13%	Apr 2015	N/A
M&G Global Dividend	1.0	3.95%	Jun 2012	N/A
Schrodgers Income Maximiser	2.0	7.94%	Jul12 / Jul15	N/A
CCLA LAMIT Property Fund	2.5	6.08%	Mar13 / Apr14	N/A
<b>Total Pooled Investment Funds</b>	<b>9.49</b>	<b>4.89%</b>		
<u>Fixed Rate Deposits (Short Term)</u>				
Close Brothers	2.0	0.65%	30 Oct 2015	29 Apr 2016
<u>Other Deposits</u>				
Funding Circle	0.3	5.00%	Apr / May 2015	N/A
<b>Total Other Deposits</b>	<b>2.3</b>			
<u>Cash Flow Investments</u>				
Insight MMF	2.7	0.50%		Instant Access
Standard Life MMF	0.75	0.50%		Instant Access
BNP Paribas MMF	3.0	0.54%		Instant Access
<b>Total Cash Flow Investments</b>	<b>6.45</b>			
<b>Total Investments at 31/03/16</b>	<b>18.24</b>			