



REPORT TO: POLICY & RESOURCES COMMITTEE ON 27 SEPTEMBER 2016

**SUBJECT: REPORT ON TREASURY MANAGEMENT PERFORMANCE AND
TREASURY AND CAPITAL INVESTMENT PRUDENTIAL
INDICATORS FOR 2015/16**

BY: CORPORATE DIRECTOR (CORPORATE SERVICES)

1. REASON FOR REPORT

- 1.1 To provide Committee with the annual outturn report on Treasury Management and details of the Council's Prudential Indicators for Treasury Management and Capital Investment for the year ended 31 March 2016.
- 1.2 This report is submitted to Committee in terms of Sections III (A) (3) of the Council's Scheme of Administration relating to Treasury Management and the Capital Plan.

2. RECOMMENDATION

- 2.1 **It is recommended that the Committee consider the Treasury Management Performance and the Council's Treasury Management and Capital Investment Prudential Indicators for 2015/16 as set out in the attached APPENDIX.**

3. BACKGROUND

- 3.1 Members have agreed that reports on Treasury Management Performance are submitted twice annually. One report to agree the Treasury Management and Investment Strategies with relevant Performance Indicators and the second report to submit the annual review and actual performance of Treasury Management activities. Quarterly Treasury Management monitoring reports are posted on the Members Portal during the year.
- 3.2 The Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector (the Code) and the Local Government Investment (Scotland) Regulations 2010. All treasury management activities are carried out in accordance with the Code and regulations.

3.3 The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy, which sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices, which set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the Council of an annual treasury management strategy report for the year ahead and an annual review report of the previous year.
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions to the Head of Financial Services as Chief Financial Officer.
- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to Policy and Resources Committee.

3.4 The Local Government (Scotland) Act 2003 requires the Council to adopt the CIPFA Prudential Code and produce prudential indicators. Each indicator either summarises the expected activity or sets limits upon the activity and reflects the outcome of the Council's underlying capital appraisal symptoms.

4. TREASURY PERFORMANCE 2015/16

4.1 This annual Treasury Management performance report covers:

- ❖ The Economy and Interest Rates in 2015/16
- ❖ Treasury Management Strategy for 2015/16
- ❖ Annual Investment Strategy 2015/16
- ❖ Investment Outturn for 2015/16
- ❖ Long Term Borrowing and Debt Rescheduling
- ❖ Short Term Borrowing
- ❖ Prudential Code for Capital Finance in Local Authorities

4.2 The Economy and Interest Rates 2015/16

4.2.1 The UK economy slowed in 2015 with GDP growth falling to 2.3% from a robust 3% the year before. Consumer Prices Inflation (CPI) inflation hovered around 0% through 2015 with deflationary spells in April, September and October 2015. The prolonged spell of low inflation was attributed to the continued collapse in the price of oil from \$67 a barrel in May 2015 to just under \$28 a barrel in January 2016. CPI picked up to 0.3% year on year in February, but this was still well below the Bank of England's 2% inflation target.

- 4.2.2 The Bank of England's Monetary Policy Committee (MPC) made no change to policy, maintaining the Bank Rate at 0.5% (in March it entered its eighth year at 0.5%) and asset purchases (Quantitative Easing) at 375bn. [The MPC reduced the Bank Rate to 0.25% on 4th August 2016].
- 4.2.3 From June 2015 gilt yields were driven lower by the weakening in Chinese growth, the knock-on effects of the fall in its stock market, the continuing fall in the price of oil and commodities and acceptance of diminishing effectiveness of central bankers' unconventional policy actions. Added to this was the heightened uncertainty surrounding the outcome of the UK referendum on its continued membership of the EU as well as the US presidential elections which resulted in significant volatility in equities and corporate bond yields.

4.3 2015/16 Treasury Management Strategy

- 4.3.1 The Treasury Management Strategy, incorporating the Annual Investment Strategy, was approved by the Council at its meeting on 12 February 2015 (Paragraph 5 of the Minute refers).
- 4.3.2 The Council's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required.
- 4.3.3 Affordability and the "cost of carry" remained important influences on the Council's borrowing strategy alongside the consideration that, for any borrowing undertaken ahead of need, the proceeds would have to be invested at rates of interest significantly lower than the cost of borrowing. As short-term interest rates have remained and are likely to remain for the foreseeable future, lower than long-term rates, it was more cost effective to mainly utilise internal borrowing and borrow short dated loans from other local authorities.
- 4.3.4 The Public Works Loan Board (PWLb) is the Council's preferred source of long-term borrowing given the transparency and control that its facilities continue to provide.

4.4 Annual Investment Strategy

- 4.4.1 Security of capital remains the Council's main investment objective followed by the desire to achieve the optimum return and the necessary liquidity. In the current economic climate it is considered to be prudent to keep investments short term and only invest with highly credited UK financial institutions who have a long-term credit rating of BBB+ or higher.
- 4.4.2 The Council's creditworthiness policy is set in accordance with credit rating criteria discussed and agreed with the Council's treasury advisers. The Head of Financial Services maintains a counterparty list in compliance with the criteria and revises the criteria and submits to Council for approval as necessary.
- 4.4.3 All credit ratings are monitored daily and the Counterparty List is amended to reflect any changes.
- 4.4.4 The transposition of European Union directives into UK legislation placed the burden of rescuing EU banks disproportionately onto unsecured institutional investors which include local authorities. This is known in the financial markets as bail-in.
- 4.4.5 The end of bank bail-outs (by governments), the introduction of bail-ins, and security being given to large numbers of depositors other than local authorities means that the risks of making unsecured deposits are much greater. Therefore the Council only deposits surplus funds with counterparties which meet the Council's minimum criteria and which offer instant access.

4.5 Investment Outturn for 2015/16

- 4.5.1 The Council manages its investments in-house and invests with the institutions listed on the Council's approved Counterparty list.
- 4.5.2 The table below shows the overall investment undertaken by the Council during 2015/16.

	Total Sum Deposited (£000)	Average Rate (%)
Approved Financial Institutions	44,565	0.53
Council's Bankers	196,808	0.40
TOTAL	241,373	0.42

The above figures are cumulative and the actual amounts invested at any one time ranged from £Nil to £17,965,000.

- 4.5.3 The average rate of interest earned on investments during the year was 0.42% compared to the average 7 day London Inter Bank Bid Rate (LIBID) of 0.44%.

4.5.4 As at 31 March 2016, the following balance was invested:

Counterparty	Investment	Amount (£000)	Interest Rate (%)
Bank of Scotland	Call Account	620	0.40

4.6 Long Term Borrowing and Debt Rescheduling

4.6.1 The Council's long term external debt position at 31 March 2016 compared with the position at the end of the last financial year was as follows: -

	31 March 2015			31 March 2016		
	Actual (£000)	Rate (%)	Average Life (Years)	Actual (£000)	Rate (%)	Average Life (Years)
Fixed Rate Funding – PWLB	122,736	5.44	22.38	129,711	5.23	20.35
Fixed Rate Funding – Market	10,100	3.95	51.40	10,100	3.95	50.40
Variable Rate Funding - PWLB	-	-		-	-	
Variable Rate Funding - Market	23,300	5.00	62.04	23,300	5.00	61.04
Total Debt	156,136	5.28		163,111	5.12	

4.6.2 The Council has been maintaining an under borrowed position which means that the capital borrowing need (Capital Finance Requirement) has not been fully funded by loan debt. Cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure to offset the need to borrow.

4.6.3 The strategy of effectively delaying new long-term borrowing by utilising internal and temporary borrowing has served well at a time when comparatively cheaper temporary borrowing from other local authorities is readily available, counterparties meeting the Council's investment criteria are limited, and historically low investment returns give rise to potentially significant carrying costs for new long-term borrowing.

- 4.6.4 During the year, the Council funded £12 million of capital expenditure by borrowing the following long-term loans from the Public Works Loan Board (PWLB).

Amount (£)	Rate (%)	Term (Years)	Repayment Type
2,000,000	1.99	10	EIP*
5,000,000	1.50	10	EIP*
5,000,000	1.84	15	EIP*

*The loans will be repaid by equal annual instalments (EIP) over the period of the loan.

- 4.6.5 No debt rescheduling was undertaken during the year as the average 1% differential between PWLB new borrowing rates and PWLB premature repayment rates continue to make rescheduling unviable.

4.7 Short Term Borrowing

- 4.7.1 During the year, seven new temporary loans totalling £15 million were raised from other UK local authorities. The following short term loans were outstanding at 31 March 2016:-

Organisation	Maturity Date	Borrowing Rate (%)	Amount £m
Western Isles Council	27 May 2016	0.50	2.00
Hartlepool Borough Council	7 June 2016	0.42	1.00
Wirral Borough Council	22 June 2016	0.50	1.00
Western Isles Council	2 August 2016	0.50	3.00
Wakefield Metropolitan Borough Council	15 November 2016	0.60	2.00
AVERAGE RATE/TOTALAMOUNT		0.51	9.00

4.8 The Prudential Code for Capital Finance in Local Authorities

- 4.8.1 The Local Government (Scotland) Act 2003 requires the Council to undertake its treasury activities with regard to the Prudential Code for Capital Finance in Local Authorities.
- 4.8.2 The Code requires the Council to produce mandatory indicators aimed at assisting members in ensuring that proposed capital investment levels and treasury management decisions satisfy the key requirements of affordability, prudence and sustainability. The Prudential Indicators for 2015/16 were approved by the Full Council on 12 February 2015 (paragraph 5 of the minute refers). There were no breaches of these indicators during 2015/16. Performance against key indicators is shown in the **APPENDIX** to this report.

5. SUMMARY OF IMPLICATIONS

(a) Moray 2026: A Plan for the Future and Moray Corporate Plan 2015 - 2017

None arising specifically from this report.

(b) Policy and Legal

The Local Government in Scotland Act 2003 provides the powers to borrow and invest as well as providing controls and limits on these activities.

The Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector which details best practice The Local Government Investment (Scotland) Regulations 2010.

All Treasury Management activities are carried out in accordance with this Code and Regulations.

(c) Financial implications

The net cost of Treasury Management activities has a significant effect on the Council's overall finances. All financial considerations are contained within the body of the report and the attached **APPENDIX**.

(d) Risk Implications

The Council is aware of the risks of passive management of the treasury portfolio and, with the support of the Council's treasury advisers, will proactively manage its investments and debt over the year.

There is little risk of volatility of costs in the current debt portfolio as the interest rates are predominantly at fixed, long term levels. Shorter term variable rates and the likely future movements in these variable rates predominantly determine the Council's investment and borrowing strategies.

Capital expenditure is closely monitored and Budget Managers are aware of their responsibilities to manage budget allocations.

(e) Staffing Implications

None arising specifically from this report.

(f) Property

None arising specifically from this report.

(g) Equalities

None arising specifically from this report.

(h) Consultations

This report has been produced in consultation with Arlingclose Limited, the Council's Treasury Advisers.

6. CONCLUSION

- 6.1 The Council's requirement for funds continues to be managed in accordance with the agreed Treasury Management Strategy Statement. All treasury management and capital investment activities have been undertaken with the limits set by the Prudential Code Performance Indicators for 2015/16.**

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Background Papers: Various working papers held within Financial Services
Ref: MW/LJC/[213-2664](#)/[213-2663](#)