



Cabinet

9 August 2017

Subject Heading:

Annual Treasury Management Report 2016/17 and proposed change to the 2017/18 Treasury Management Strategy Statement

Cabinet Member:

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Policy context:

The code of practice on treasury management 2009 requires a year end report to Full Council on the treasury management. Recommended changes to the Treasury Management Strategy also requires approval by Full Council

Financial summary:

There are no direct financial implications from the report. The changes requested to the Treasury Management Strategy will enable more flexibility in investment decisions going forward. The financial implications of all investment decisions will be considered as part of robust due diligence procedures taken in line with the Strategy and established processes and procedures.

Is this a Key Decision?

No

Is this a Strategic Decision

Yes

When should this matter be reviewed?

N/A

Reviewing OSC:

N/A

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[X]
Places making Havering	[X]
Opportunities making Havering	[X]
Connections making Havering	[X]

SUMMARY

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 to Full Council at least twice yearly (mid-year and at year end).

The Authority has borrowed and invested 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, its associated monitoring and control of risk.

In 2016/17 there was no new long term borrowing, while external investment income outturn exceeded the budgeted figure by £0.509m was achieved despite the Bank of England bank rate cut in August 2016 from 0.5% to 0.25% and the benchmark LIBOR falling from 0.50% in Q2 to 0.44% at 31/3/17.

RECOMMENDATIONS

That Cabinet:

1. **Note** the final 2016/17 Treasury Position set out in this report.
2. **Note** the treasury and prudential indicators as set out in **Appendix 3** of this report: and
3. **Recommend** to Full Council to consider this report and approve the proposed changes to the 2017/18 Treasury Management Strategy Statement (TMSS) as set out in **Appendix 4**.

REPORT DETAIL

Contents

1. Annual Investment Strategy
2. New Borrowing
3. Debt Rescheduling

4. Compliance with Treasury Indicators
5. Compliance with Prudential Indicators; and
6. Other Treasury Related Matters.

1. Annual Investment Strategy

1.1 The 2016/17 TMSS was approved by the Authority in February 2016 and sets out the investment priorities in order of priority as:

- Security of Capital
- Liquidity; and
- Yield.

1.2 The Authority will aim to achieve the optimum return (yield) on investments commensurate with acceptable levels of security and liquidity.

1.3 The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. As a result of investing these cash balances, the Authority is exposed to financial risks and the revenue effect of changing interest rates. A breakdown of deposits held in 2016/17 is shown in appendix 1 while investment performance is shown in table 1 below:

Table 1: Investment performance for 2016/17

Benchmark	Benchmark Return %	Budgeted Rate of Return %	Actual Rate of Return %	Investment interest Earned* (£'m)
Quarter 1	0.58	0.60	0.77	0.237
Quarter 2	0.51	0.60	0.76	0.478
Quarter 3	0.47	0.60	0.69	0.923
Quarter 4	0.44	0.60	0.72	1.469

*interest on external investments.

* Figures changed slightly from Q4 report given outturn figures (subject to audit) have now been established. .

1.4 The UK Bank Rate fell to 0.25% in August 2016 from 0.50% since March 2009, keeping short-term money market rates at historically low levels.

1.5 As illustrated in Table 1, at Q4 the Authority outperformed the benchmark by 0.28% and the budgeted rate of return by 0.12%. The external investment interest earned was £1.469m compared to the budget of £0.960m.

1.6 The Authority had £212.7m of loans (long and short term loans) and £200.9m of investments at year end. This is summarised in Table 2 below and detailed in appendix 2.

Table 2 – Existing Investment & Debt Portfolio Position

	31/03/2017 Actual Portfolio £m	31/03/2017 Average Rate %
Long Term Borrowing:		
PWLB – Fixed Rate	203.234	
PWLB – Variable Rate	-	
Local Authorities	-	
LOBO Loans	7.000	
Other*	1.339	
Total Long Term Borrowing	211.573	3.59
Short Term Borrowing		
Local Authorities	2.250	
Other	0.262	
Total Short Term Borrowing	2.512	0.43
Investments:		
Short-term investments	160.904	
Long-term investments	40.000	
Total Investments	200.904	0.71
Net Borrowing/ Investments	13.181	

*Energy efficiency loan.

2. New borrowing

- 2.1 Affordability and the “cost of carry” remain important influences on the Authority’s borrowing strategy alongside the consideration that, for any borrowing undertaken ahead of need, the proceeds would have to be invested in the money markets at rates of interest significantly lower than the cost of borrowing.
- 2.2 As short-term interest rates are likely to remain below long-term borrowing rates, it is more cost effective in the short-term to use internal resources instead although this will be kept under constant review and will respond to opportunities and changing forecasts as they arise.
- 2.3 In 2016/17, no new long term borrowing was undertaken to fund capital expenditure. Future capital spending plans are regularly reviewed and any additional long term borrowing will only be taken after careful consideration of affordability, revenue impact, direction in travel of interest rates, the

Authority's capital programme requirement and advice from the Treasury Adviser.

- 2.4 During 2017/18 a fundamental review of the Authority's capital investment plans is being undertaken in order to develop a 5 year capital programme from 2018/19 to 2023/24. The programme will be developed to align with the Corporate Plan priorities, optimise the use of external funding streams and ensure that any further borrowing to fund future capital investment plans is affordable over the long term in revenue terms.

3. Debt Rescheduling

- 3.1 The opportunities for debt rescheduling are regularly reviewed by the Authority's treasury adviser in consultation with senior treasury officers, the S151 officer and lead Cabinet Member for Finance.
- 3.2 The PWLB continued to operate a spread of approximately 1% between "premature repayment rate" and "new loan" rates so the premium charge for early repayment of PWLB debt remained relatively expensive for loans in the Authority's portfolio and prevented any debt rescheduling activity in 2016/17.

4. Treasury and Prudential Indicators

- 4.1 Appendix 3 shows treasury activity compared with the Authority's approved Treasury and Prudential Indicators (affordability limits) for 2016/17 as set out in the approved TMSS.

5. Other Treasury related Matters

5.1 Policy on Use of Financial Derivatives

- 5.1.1 The Authority has not entered into any stand alone financial derivatives during the financial year 2016/17.

5.2 Policy on Apportioning Interest to the HRA

- 5.2.1 The Authority has apportioned interest to the HRA at 0.50%. All the risks associated with treasury activities (which are kept to a minimum through the Authority's TMSS) lie with the General Fund rather than the HRA. This rate will be reviewed in 2017/18.

5.3 Investment Training

- 5.3.1 The needs of the Authority's treasury management staff for training in investment management are assessed every year as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.

5.3.2 During 2016/17 staff attended training courses, seminars and conferences provided by the Treasury Adviser, CIPFA and other treasury organisations. In addition treasury management staff also attended the London Treasury Officers Forum, a group set up for networking and sharing best practice.

5.4 Investment Advisers

5.4.1 The Authority appointed Arlingclose Limited as treasury management advisers. Throughout the course of the year officers receive on a daily basis specific advice on investment, debt and capital finance issues augmented by a quarterly strategy review meeting with the S151 officer and the lead Member for Finance.

5.5 Security

5.5.1 Security of capital remains the Authority's overriding investment objective and is delivered through the Authority's counterparty policy as set out in its TMSS 2016/17.

5.5.2 Counterparty credit quality was assessed and monitored with reference to credit ratings (using the ratings from all three of the main credit rating agencies Fitch, S&P and Moody's); for financial institutions analysis of funding structure and susceptibility to bail-in, credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. During the financial year none of the banks on the Authority's lending list failed the stress tests conducted by the European Banking Authority in July 2016 and by the Bank of England in November 2016.

5.5.3 The Authority has also made use of secured investments products that provide collateral in the event that the counterparty cannot meet its obligations for repayment as additional security for its deposits.

6.0 Proposed Changes to the 2017/18 TMSS

6.1 Officers and the Treasury Adviser constantly scan the market to identify suitable investment opportunities and with investment rates remaining lower for longer and CPI inflation increasing, the need to do this is ever more important if investment income budget targets are to be met.

6.2 This point was made in the Q4 report to Audit Committee and the proposed changes are requested so that Officers have scope to investigate investments that will provide higher returns than are currently available in the strategy but without compromising the aforementioned investment objectives. Examples of such investments are: asset backed solar bonds and pooled funds.

- 6.3 The Cabinet is being asked to recommend to Full Council to consider the report and approve changes to the 2017/18 TMSS amendments to enable the Authority to invest in unrated, secured corporate bonds and increase the limit on pooled fund investments. These amendments are set out in appendix 4 of this report.

REASONS AND OPTIONS

Reasons for the decision:

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 to Full Council at year end.

Other options considered:

The other option would be to not report the performance of the treasury function and request approval of the amendments to the 2017/18 Treasury Management Strategy however as this would be in breach of CIPFA's TM Code, this was not considered.

IMPLICATIONS AND RISKS

Financial implications and risks:

There are no direct financial implications from this report. The financial implications of future treasury decisions will be considered within the financial governance framework of the TMSS and its established processes and procedures to ensure the investment objectives are achieved.

Legal implications and risks:

The Local Authority has a power to invest in virtue of section 12 Local Government Act 2003 (a) for any purpose relevant to its functions under any enactment, or (b) for the purposes of the prudent management of its financial affairs. The Authority must have regard to relevant guidance which in this case is provided by CIPFA. Otherwise there are no apparent legal implications or risks from this report.

Human Resources implications and risks:

There are no HR implications from this report

Equalities implications and risks:

There are no Equalities implications arising from this report

BACKGROUND PAPERS

None