POLICY, RESOURCES & GROWTH COMMITTEE	Agenda Item 8 Brighton & Hove City Council

Subject:		**Treasury Management Policy Statement 2015/16 – End of year review**	
Date of Meeting:		**13 July 2017**	
Report of:		**Executive Director of Finance & Resources**	
Contact Officer:	**Name:**	**James Hengeveld**	**Tel: 01273 29-1242**
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Ward(s) affected:		**All**	

FOR GENERAL RELEASE

1. PURPOSE OF REPORT AND POLICY CONTEXT

1.1 The 2016/17 Treasury Management Policy Statement (TMPS), practices, and schedules were approved by the Policy & Resources Committee on 17 March 2016. The TMPS sets out the role of Treasury Management, whilst the practices and schedules set out the annual targets and methods by which these targets will be met.

1.2 The TMPS includes the Annual Investment Strategy (AIS) which sets out the key parameters for investing council cash balances and was approved by Full Council on 24 March 2016.

2. RECOMMENDATIONS:

2.1 That Policy, Resources & Growth Committee endorses the key actions taken during the second half of 2016/17 to meet the TMPS and practices (including the investment strategy) as set out in this report.

2.2 That Policy, Resources & Growth Committee notes the reported compliance with the AIS for the period under review.

2.3 That Policy, Resources & Growth Committee notes that the approved maximum indicator for investment risk of 0.05% has been adhered to and the authorised borrowing limit and operational boundary have not been exceeded.

3. CONTEXT/ BACKGROUND INFORMATION

Overview of the markets

3.1 2016/17 saw a number of unusual world events which has impacted on the domestic and global economy. The EU Referendum in June 2016 saw the UK vote to leave the EU resulting in a significant deflation of sterling and led to the Bank of England cutting interest rates to 0.25% in August 2016 as a result of what the central bank forecast to be a sharp slowdown in growth in the second half of 2016. The US presidential election in November 2016 resulted in the triumph of Donald Trump which forced markets to assess the market and economic impact of a potential revision to US economic, trade and foreign policy.

There have also been geo-political tensions during the year which has affected both global and domestic economic stability and market sentiment.

3.2 A fresh layer of uncertainty has been added on the domestic front following the 8th June election result. Sterling slipped further whilst other markets struggled to interpret the impact of the outcome of the election. On 21 June 2017 the Queen's Speech took place as she announced 27 bills to Parliament. Unsurprisingly, Brexit negotiations will make up the majority of the legislation planned for the next two years, but there will also be a greater focus on counter-terrorism plans, infrastructure projects and the economy. Negotiations are now underway to decide upon the terms of the UK exiting the EU. The terms of exit are crucial to the market's view of the future of the UK economy and negotiations will be carefully watched and interpreted by markets.

3.3 Interest rates have remained at historical lows, but inflation has surged to its highest point in four years following the fall in sterling. The Bank of England's Monetary Policy committee (MPC) meeting in June surprised markets and commentators with a 5-3 vote to keep interest rates unchanged, with three members calling for a rate rise. MPC Member Andy Haldane suggested after the Queen's speech that he considered voting for a rate rise in the meeting. This comes as some surprise given that his stance is usually more dovish[1]; whilst Bank of England Governor, Mark Carney, had expressed on 20 June 2017 that now was not the right time to raise interest rates due to uncertain consumer spending, business investment and wage growth. There has been some volatility in the markets as they interpret the MPC vote and comments around rate rises.

3.4 There are many uncertainties which will weigh on the prospects of interest rates going forward. These include the negotiations over the terms of the UK exiting the EU, the breadth of US economic and trade policy and geo-political concerns.

Treasury Management Strategy

3.5 A summary of the action taken in the 6 months to March 2017 is provided in Appendix 1 to this report and further information on borrowing and investment performance is shown in the March 2017 Bulletin at Appendix 2. The main points are:

- The council entered into no new borrowing duringThe the period;
- The highest risk indicator during the period was 0.039% which is below the maximum set of 0.050%;
- The return on investments by the in-house team and cash manager have exceeded the target rates;
- The two borrowing limits approved by full Council have not been exceeded.

3.6 Treasury management activity for the half-year has focused on a short-term horizon as summarised in the table below:

[1] Dovish: Less inclined to take aggressive measures in relation to unfavourable movements in inflation or other factors (opposite of Hawkish).

	Amount invested 1 Oct 2016 to 31 Mar 2017			
	Fixed deposits	Money market funds	Total	
Up to 1 week	-	£271.5m	£271.5m	93%
Between 1 week & 1 month	-	-	-	0%
Between 1 month & 3 months	-	-	-	0%
Over 3 months	£20.5m	-	£20.5m	7%
	£20.5m	**£271.5m**	**£292.0m**	**100%**

Budget versus Outturn 2016/17

3.7 The following table summarises the performance achieved on investments compared to the budgeted position and approved benchmark for the whole year.

	In-house Investments		Cash Manager investments (net of fees)	
	Average Balance	Average rate	Average Balance	Average rate
Budget 2016/17	£66.1m	0.60%	£25.7m	1.00%
Actual 2016/17	£94.5m	0.72%	£25.9m	0.87%
Benchmark Rate		0.20%		0.23%

3.8 The Financing Costs budget variance in 2016/17 was £0.478m underspent. This is made up of a number of variances. The key savings include an over-achievement of investment income of £0.287m as a result of both higher balances (partly due to bringing forward borrowing into 2016/17 from future years), and achievement of higher investment rates than budgeted. A further £0.269m one off saving was achieved as part of the conclusion of the council's review of its Minimum Revenue Provision policy. A further £0.080m was achieved as a result of a budget for contributions to trusts not being required as this was already accounted for in a separate budget line.

3.9 These savings have been offset by additional net borrowing costs of £0.147m as a result of bringing forward borrowing to take advantage of historically low borrowing rates. This is expected to make permanent savings of £0.086m per year, which has been built into the Financing Costs budget for 2017/18 onwards.

Summary of Treasury Activity October 2016 to March 2017

3.10 The following table summarises the treasury activity in the half year to March 2017 compared to the corresponding period in the previous year:

October to March	2014/15	2015/16	2016/17
Long-term borrowing raised (i360)	(£9.2m)	(£8.5m)	-
Long-term borrowing raised (General Fund)	-	(£15.0m)	-
Long-term borrowing raised (HRA)	-	-	-
Long-term borrowing repaid (i360)	-	£0.3m	£0.5m
Long-term borrowing repaid (General Fund)	-	-	-
Long-term borrowing repaid (HRA)	£3.9m	£3.0m	-
Short-term borrowing repaid	-	£1.0m	£1.0m
Investments made	£303.5m	£277.6m	£292.0m
Investments maturing	(£318.4m)	(£286.4m)	(£306.2m)

3.11 The following table summarises how the day-to-day cash flows in the second half-year have been funded compared to the same period in the previous year:

October to March	2014/15	2015/16	2016/17
Net cash flow (shortage)/surplus	**(£19.6m)**	**(£27.2m)**	**(£12.9m)**
Represented by:			
Increase/(reduction) in long-term borrowing	£5.3m	£20.2m	(£0.5m)
Increase/(reduction) in short-term borrowing*	-	(£1.0m)	(£1.0m)
Reduction/(increase) in investments	£14.9m	£8.8.m	£14.2m
Reduction/(increase) in bank balance	(£0.6m)	(£0.8m)	£0.2m

*South Downs National Park

Security of Investments

3.12 A summary of investments made by the in-house team and outstanding as at 31 March 2017 in the table below shows that investments continue to be held in good quality, short term instruments. The funds invested in BBB institutions included in the table below are invested in the part-nationalised banks which are backed by Government guarantees in line with the AIS.

‘AAA’ rated money market funds	£11.20m	18%
‘AA’ rated institutions	£6.00m	9%
‘A’ rated institutions	£46.50m	73%
‘BBB’ rated institutions	-	0%
Total	**£63.25m**	**100%**
Period – less than one week	£11.20m	18%
Period – between one week and one month	£4.50m	7%
Period – between one month and three months	£9.04m	14%
Period – between three months and 1 year	£38.51m	61%
Total	**£63.25m**	**100%**

Risk

3.13 As part of the investment strategy for 2016/17 the Council agreed a maximum risk benchmark of 0.050% i.e. there is a 99.95% probability that the council will get its investments back. The benchmark is a simple target that measures the risk based on the financial standing of counterparties and length of each investment based on historic default rates. The actual risk indicator has varied between 0.019% and 0.039% between October 2016 and March 2017. It should be remembered however that the benchmark is an ‘average risk of default’ measure, and does not constitute an expectation of loss against a particular investment.

3.14 The treasury management service is subject to detailed audit each year. This includes the testing of the control environment and the management of risk. A reasonable level of assurance was provided during the most recent audit (February 2016) and all recommendations have been implemented.

Compliance with the Annual Investment Strategy

3.15 During the reporting period, the information in this report provides assurance that the Annual Investment Strategy has been complied with in full.

Borrowing Strategy

3.16 Over recent years the council has been following a strategy of repaying debt and funding its borrowing requirement through utilising cash balances which were supporting the council’s reserves and balances. This is a prudent strategy which has allowed the council to reduce the impact of the difference in the cost of borrowing compared with the income received from investments, and reduce its counterparty exposure risk. The approved strategy for 2015/16 included a change in approach as a result of a number of contributing factors; an expectation of increases in interest rates in the following year, the expected reduction of certain reserves over the next 4 years, and the forward borrowing opportunities expected in the local authority market. A total of £20m of new borrowing was included in the Financing Costs budget to be taken on in £5m tranches from 2016/17 to 2019/20.

3.17 The forward borrowing opportunities did not become available, which coincided with historic falls and significant volatility in PWLB interest rates. Following analysis of borrowing costs and interest rate forecasts, and in consultation with the council’s Treasury Advisors, “trigger” rates were set and met during 2015/16, resulting in a total of £10m of borrowing being bought forward into 2015/16. Further trigger rates were set (and met) in 2016/17 as low interest rates and volatility continued, and permanent savings were able to be made by taking on the further £10m borrowing requirement earlier.

3.18 Undertaking the total of £20m borrowing in 2015/16 and 2016/17 at historically low rates has enabled the General Fund to achieve a total of £0.105m permanent revenue savings.

3.19 A summary of the council’s debt portfolio following these changes is summarised in Appendix 1.

Treasury Advisors

3.20 The council has a three year contract for treasury advisory services with Capita Asset Services (CAS) to November 2018. The Capita Group announced on 23 June 2017 that the group had exchanged contracts with Link Administration Holdings (the “Link Group”) for the disposal of CAS. The sale is expected to complete in Q4 of 2017. Link Group is an international provider of financial administration solutions, with significant presence throughout Australasia, Asia, Africa, the Middle East and Europe.

4. ANALYSIS & CONSIDERATION OF ANY ALTERNATIVE OPTIONS

4.1 This report sets out action taken in the 6 months to March 2017. Treasury management actions have been carried out within the parameters of the AIS, TMPS, and Prudential Indicators. Therefore no alternative options have been considered.

5. COMMUNITY ENGAGEMENT & CONSULTATION

5.1 The council's external treasury advisors have been consulted over the content of this report. No other consultation has been undertaken.

6. CONCLUSION

6.1 Treasury management is governed by a code that is recognised as "best and proper practice" under the Local Government Act 2003. The Code requires a minimum of two reports per year, one of which is required to review the previous year's performance. This report fulfils this requirement.

7. FINANCIAL & OTHER IMPLICATIONS:

Financial Implications:

7.1 The financial implications of treasury management activity are reflected in the financing costs budget set out in paragraph 3.7 to 3.9.

Finance Officer Consulted: James Hengeveld Date: 20/6/17

Legal Implications:

7.2 The TMPS and associated actions are exercised under powers given to the council by Part 1 of the Local Government Act 2003 which includes the power for a local authority to invest for the purposes of the prudent management of its financial affairs (section 12).

7.3 The Council's policy and the actions outlined in the report are consistent with the Council's obligations under the Act and with good financial practice.

Lawyer Consulted: Victoria Simpson Date: 19/06/17

Equalities, Sustainability and other significant implications:

7.4 There are no direct implications arising from this report.

SUPPORTING DOCUMENTATION

Appendices

1. A summary of the action taken in the period October 2016 to March 2017

2. March 2017 Treasury Management Statistics

Documents in Members' Rooms

None.

Background Documents

1. Part I of the Local Government Act 2003 and associated regulations.

2. The Treasury Management Policy Statement and associated schedules 2016/17 approved by Policy & Resources on 17 March 2016.

3. The Annual Investment Strategy 2016/17 approved by full Council on 24 March 2016.

4. Treasury Management Policy Statement 2016/17 (including Annual Investment Strategy 2016/17) – Mid-Year Review approved by Policy & Resources Committee on 8 December 2016.

5. Papers held within Financial Services, Finance & Resources Directorate.

6. The Prudential Code for Capital Finance in Local Authorities published by CIPFA 2011.