

<b>Subject:</b>	<b>Treasury Management Policy Statement 2013/14 – End of year review</b>		
<b>Date of Meeting:</b>	<b>11 July 2014</b>		
<b>Report of:</b>	<b>Executive Director of Finance &amp; Resources</b>		
<b>Contact Officer:</b>	<b>Name:</b>	<b>James Hengeveld</b>	<b>Tel: 29-1242</b>
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<b>Ward(s) affected:</b>	<b>All</b>		

**FOR GENERAL RELEASE**

**1. PURPOSE OF REPORT AND POLICY CONTEXT**

- 1.1 The 2013/14 Treasury Management Policy Statement (TMPS), practices and schedules were approved by Policy & Resources on 21 March 2013. 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 funds and was approved by Full Council on 28 March 2013 and amended by full Council on 12<sup>th</sup> December 2013.
- 1.3 It is recommended good and proper practice that Members receive half yearly reports and review and endorse treasury management actions during the year. The mid-year review was presented to Policy and Resources on 5<sup>th</sup> December 2013.

**2. RECOMMENDATIONS:**

- 2.1 That Policy & Resources Committee endorses the key actions taken during the second half of 2013/14 to meet the treasury management policy statement and practices (including the investment strategy) as set out in this report.
- 2.2 That Policy & Resources Committee notes that the approved maximum indicator for investment risk of 0.05% has been adhered to and the authorised limit and operational boundary have not been exceeded.

**3. CONTEXT/ BACKGROUND INFORMATION**

***Overview of Markets***

- 3.1 The financial year 2013/14 continued the challenging investment environment of previous years, namely low investment returns, although levels of counterparty risk had subsided somewhat. Economic growth (GDP) in the UK was virtually flat during 2012/13 but surged strongly during the 2013/14. Consequently there was no additional quantitative easing during 2013/14 and Bank Rate ended the year unchanged at 0.5% for the fifth successive year. There is much speculation that

the base rate may increase later this year but the Governor of the Bank of England has made it clear that any increase will be small and further increases will happen slowly. While CPI inflation had remained stubbornly high and substantially above the 2% target during 2012, by January 2014 it had, at last, fallen below the target rate to 1.9%. In April, CPI had fallen to 1.5% however it is also expected to remain slightly below the target rate for most of the two years ahead.

3.2 The Funding for Lending Scheme, announced in July 2012, resulted in a flood of cheap credit being made available to banks which then resulted in money market investment rates falling drastically in the second half of that year and continuing into 2013/14. That part of the Scheme which supported the provision of credit for mortgages was terminated in the first quarter of 2014 as concerns rose over resurging house prices.

3.3 The EU sovereign debt crisis subsided during the year and confidence in the ability of the Eurozone to remain intact increased substantially. Perceptions of counterparty risk improved after the ECB statement in July 2012 that it would do “whatever it takes” to support struggling Eurozone countries; this led to a return of confidence in its banking system which has continued into 2013/14 and led to a move away from only very short term investing. However, this is not to say that the problems of the Eurozone, or its banks, have ended as the zone faces the likelihood of weak growth over the next few years at a time when the total size of government debt for some nations is likely to continue rising.

#### ***Treasury Management Strategy***

3.4 A summary of the action taken in the six months to March 2014 is provided in Appendix 1 to this report and further information on borrowing and investment performance is shown in the end of year Bulletin at Appendix 2. The main points are:

- The council did not enter into any new borrowing arrangements during the period;
- The highest risk indicator during the period was 0.018% which is well below the maximum set of 0.05%;
- The return on investments by the in-house treasury team and cash manager has exceeded the target rates.
- The two borrowing limits approved by full Council have not been exceeded.

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

	Amount invested 1 <sup>st</sup> Oct 2013 to 31 Mar 2014			
	Fixed deposits	Money market funds	Total	
Up to 1 week	£2.3m	£193.1m	£195.3m	71%
Between 1 week & 1 month	£7.0m	£3.0m	£10.0m	4%
Between 1 month & 3 months	£38.5m	£22.5m	£61.0m	22%
Over 3 months	£8.0m	-	£8.0m	3%
	<b>£55.8m</b>	<b>£218.6m</b>	<b>£291.2m</b>	<b>100%</b>

### **Budget vs Outturn 2013/14**

- 3.6 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)	
	Aver Bal	Aver rate	Aver Bal	Aver rate
Budget 2013/14	£52.9m	0.63%	£24.6m	0.75%
Actual 2013/14	£78.9m	0.51%	£24.9m	0.82%
Benchmark Rate		0.36%		0.36%

- 3.7 The Financing Costs budget has seen higher than anticipated cash balances, offset in part by lower than anticipated investment rates. This, combined with the funding of large projects (such as The Keep and the Workstyles project) temporarily from internal reserves as opposed to external borrowing, has resulted in a net saving of £0.2m to the Financing Costs budget. The council will eventually have undertake external borrowing to fund these projects at a time when market conditions are assessed to be optimal. The underspend has therefore been transferred to the Financing Costs reserve which covers future borrowing and investment rate risks.

### **Summary of Treasury activity October 2013 to March 2014**

- 3.8 The table below summarises the treasury activity in the half-year to March 2014 with the corresponding period in the previous two years.

October to March	2011/12	2012/13	2013/14
Long-term borrowing raised – Capital	£10.0m	-	-
Long-term borrowing raised – HRA	£18.1m	-	-
Long-term borrowing repaid	-	-	-
Short-term borrowing raised	-	-	-
Short-term borrowing repaid	-	-	-
Investments made	£316.7m	£313.7m	£274.3m
Investments maturing	(£320.0m)	(£359.8m)	(£291.2m)

- 3.9 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 two years.

October to March	2011/12	2012/13	2013/14
Cash flow shortage – general	-£13.0m	-£34.9m	-£23.8m
HRA Settlement Payment	-£18.1m	-	-
<b>Net cashflow shortage/surplus</b>	<b>-£31.1m</b>	<b>-£34.9m</b>	<b>-£23.8m</b>
Represented by:			
Increase in long-term borrowing	+£28.1m	-	-
Change in short-term borrowing	-	*-£2.0m	*£2.0m
Change in investments	£3.3m	£37.5m	£16.9m
Change in bank balance	-£0.3m	-£0.6m	£4.9m

\*South Downs National Park

### ***Security of Investments***

- 3.10 A summary of investments made by the in-house treasury team and outstanding as at 31 March 2014 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 guarantee in line with the AIS.

'AAA' rated money market funds	£10.61m	20%
'A' rated institutions	£17.01m	32%
'BBB' rated institutions	£24.90m	47%
<b>Total</b>	<b>£52.52m</b>	<b>100%</b>
Period – less than one week	£26.27m	50%
Period – between one week and one month	£8.00m	15%
Period – between one month and three months	£5.01m	10%
Period – between three months and six months	£9.24m	18%
Period – between 6 months and 1 year	£4.00m	8%
<b>Total</b>	<b>£52.52m</b>	<b>100%</b>

### ***Municipal Bonds Agency Investment***

- 3.11 The Local Government Agency's (LGA's) is developing a new initiative, the Municipal Bonds Agency (MBA). Currently, 75% of Local Authority borrowing is sourced from the government's Public Works Loans Board (PWLB). The establishment of a Bonds Agency will potentially inject some competition and diversity into the Local Authority borrowing marketplace. Additionally, the MBA estimates that once established, councils will be able to access borrowing at rates that could be somewhat lower than the PWLB borrowing rates. At this stage it is not clear whether this will be suitable for future long term borrowing by the Council and this will be assessed as more information becomes available.
- 3.12 The LGA is currently looking for Local Authorities to provide equity investments in the MBA. An equity investment will help enable the establishment of the MBA, which will allow the council to benefit from lower future borrowing rates. However, there are associated risks with the investment which must be treated as capital expenditure, and there is a considerable amount of due diligence work required before an investment is recommended. Officers are meeting with the LGA in July 2014 to discuss the initiative further.
- 3.13 The Targeted Budget Management (TBM) Month 2 report included elsewhere on this agenda recommends that Policy and Resources delegate the authority of entering into a £50,000 equity investment into the Municipal Bonds Agency to the Executive Director of Finance and Resources in consultation with the Chair of Policy and Resources Committee and Opposition Leaders if further investigation demonstrates that the investment is sound.

### ***Risk***

- 3.14 As part of the investment strategy for 2013/14 the Council agreed a maximum risk benchmark of 0.05% 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 0.009% and 0.018% between October 2013 and March 2014. 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.

- 3.15 In January 2014, Internal Audit and Business Risk undertook an audit of the treasury management function. The audit concluded that “substantial assurance” is provided on the effectiveness of the control framework operating and mitigating risks for treasury management.

#### **4. ANALYSIS & CONSIDERATION OF ANY ALTERNATIVE OPTIONS**

- 4.1 This report sets out action taken in the six months to March 2014. 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 was necessary.

#### **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 3.6.

*Finance Officer Consulted: James Hengeveld*

*Date: 17/06/14*

##### 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).

*Lawyer Consulted: Oliver Dixon*

*Date: 18/06/14*

##### Equalities, Sustainability and other significant implications:

7.3 There are no direct implications arising from this report.

## **SUPPORTING DOCUMENTATION**

### **Appendices:**

1. A summary of the action taken in the period October 2013 to March 2014
2. March 2014 Treasury Management Bulletin

### **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 2013/14 approved by Policy & Resources on 21 March 2013
3. The Annual Investment Strategy 2013/14 approved by full Council on 28 March 2013
4. Treasury Management Policy Statement 2013/14 (including Annual Investment Strategy 2013/14) – End of year Review approved by Policy & Resources Committee on 5 December 2013 and full Council on 12 December 2013
5. Papers held within Financial Services, Finance & Resources Directorate
6. The Prudential Code for Capital Finance in Local Authorities published by CIPFA 2011