2014 / 15 TREASURY OPERATIONS ANNUAL PERFORMANCE REVIEW

Committee: Finance and Governance Committee

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[Q76]

1.0 ISSUE

1.1 To report on the Council's treasury operations during 2014/15.

1.2 The report reviews the treasury management activity during the financial year 2014/15 and reports on the prudential indicators as required by CIPFA's Treasury Management Code of Practice.

1.3 Investments totalled £15.440 million as at 31 March 2015, an increase of £2.557 million on the previous year. The Council's cash investments are still for periods of less than one year.

1.4 Interest received during the financial year was £145,046 which was £45,046 above the budget of £100,000.

1.5 The average rate of return was 0.59%, a slight decrease from the 2013/14 figure of 0.69%. This was still above the benchmark three month LIBID (London Inter-bank Bid Rate) of 0.47%.

2.0 RECOMMENDATIONS

2.1 That Members note the contents of the report and to recommend to Full Council the report on the Council's treasury operations during 2014/15, including the prudential and treasury indicators, as set out at Appendix 1.

2.2 That the members note that the Treasury management strategy will be revised as proposals are made for the funding implications of the leisure centre and the LATC, these changes will need to be approved by the full council.

3.0 BACKGROUND / INTRODUCTION

3.1 This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2014/15. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

3.2 The Treasury Management Policy Statement

As per CIPFA's definition, the Council defines its treasury management activities as:

- The management of the Council's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.
- The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council, and any financial instruments entered into to manage these risks.
- The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

The Council will create and maintain, as the cornerstones for effective treasury management:

- A treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities
- Suitable treasury management practices (TMPs), setting out the manner in which the Council will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities
- The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of this Council. Such amendments will not result in the Council materially deviating from the Code's key principles.
- Full Council will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.
- The Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Finance and Governance Committee, and for the execution and administration of treasury management decisions to

the Head of Finance, who will act in accordance with the Council's policy statement and TMPs and, if a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

- The Council nominates Finance and Governance Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

During 2014/15 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 26/02/2014)
- a mid-year (minimum) treasury update report (Council 04/12/2014)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

3.3 The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

3.4 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

3.5 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans, or using longer-term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

3.6 The council is required to approve Annual Treasury reports.

3.7 This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Committee before they were reported to the full Council.

3.8 No training was offered in the year.

4.0 The Economy and Interest Rates

4.1 The original market expectation at the beginning of 2014/15 was for the first increase in Bank Rate to occur in quarter 1 2015 as the unemployment rate had fallen much faster than expected through the Bank of England's initial forward guidance target of 7%. In May, however, the Bank revised its forward guidance. A combination of very weak pay rises and inflation above the rate of pay rises meant that consumer disposable income was still being eroded and in August the Bank halved its forecast for pay inflation in 2014 from 2.5% to 1.25%. Expectations for the first increase in Bank Rate therefore started to recede as growth was still heavily dependent on buoyant consumer demand. During the second half of 2014 financial markets were caught out by a halving of the oil price and the collapse of the peg between the Swiss franc and the euro. Fears also increased considerably that the ECB was going to do too little too late to ward off the threat of deflation and recession in the Eurozone. In mid-October, financial markets had a major panic for about a week. By the end of 2014, it was clear that inflation in the UK was going to head towards zero in 2015 and possibly even turn negative. In turn, this made it clear that the MPC would have great difficulty in starting to raise Bank Rate in 2015 while inflation was around zero and so market expectations for the first increase receded back to around quarter 3 of 2016.

4.2 Gilt yields were on a falling trend for much of the last eight months of 2014/15 but were then pulled in different directions by increasing fears after the anti-austerity parties won power in Greece in January; developments since then have increased fears that Greece could be heading for an exit from the euro. While the direct effects of this would be manageable by the EU and ECB, it is very hard to quantify quite what the potential knock on effects would be on other countries in the Eurozone once the so called impossibility of a country leaving the EZ had been disproved. Another downward pressure on gilt yields was the announcement in January that the ECB would start a major programme of quantitative easing, purchasing EZ government and other debt in March. On the other hand, strong growth in the US caused an increase in confidence that the US was well on the way to making a full recovery from the financial crash and would be the first country to start increasing its central rate, probably by the end of 2015. The UK would be closely following it due to strong growth over both 2013 and 2014 and good prospects for a continuation into 2015 and beyond. However, there was also an increase in concerns around political risk from the general election due in May 2015.

5.0 Overall Treasury Position as at 31 March 2015

5.1 At the beginning and the end of 2014/15 the Council's treasury position was as follows:

Table 1	31 March 2014 Actual		31 March 2015 Actual
Total debt	***£0.00m***		***£0.00m***
CFR	***£0.62m***		***£0.20m***
Over / (under) borrowing	***£0.034m***		***(£0.041m)***
Total investments	***£12,548m***		***£13,017m***

These investment figures represent revenue reserves, capital receipts, S106 and working balances.

The difference in investment figure for year ending 2015 can be attributed to increase in revenue reserves.

6.0 **The Strategy for 2014/15**

6.1 The expectation for interest rates within the strategy for 2014/15 anticipated low but rising Bank Rate (starting in quarter 1 of 2015), and gradual rises in medium and longer term fixed borrowing rates during 2014/15. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

6.2 This council's priority is firstly security of investment, cashflow and then returns on investment, which is still been adhered to .

6.3 In this scenario, the treasury strategy was to postpone borrowing to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

6.4 The actual movement in gilt yields meant that PWLB rates saw little overall change during the first four months of the year but there was then a downward trend for the rest of the year with a partial reversal during February.

6.5 Treasury management activity was within the prudential indicators and treasury management indicators.

7.0 **The Borrowing Requirement and Debt**

7.1 The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR).

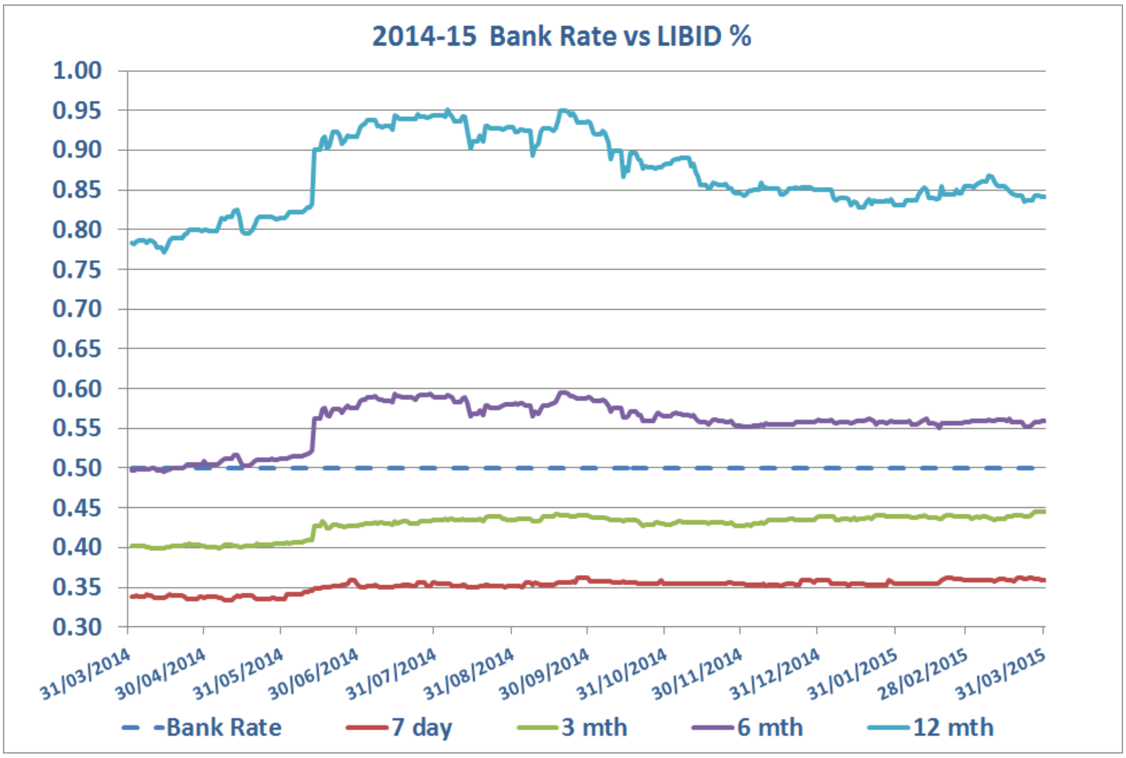
	31 March 2014 Actual	31 March 2015 Budget	31 March 2015 Actual
Total CFR	0.62	0.62	0.20

8.0 **Borrowing Outturn for 2014/15**

8.1 No borrowing was undertaken during the year.

9.0 **Investment Rates in 2014/15**

9.1 Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for six years. Market expectations as to the timing of the start of monetary tightening started the year at quarter 1, 2015 but then moved back to around quarter 3, 2016 by the end of the year. Deposit rates remained depressed during the whole of the year, primarily due to the effects of the Funding for Lending Scheme.



10.0 **Investment Outturn for 2014/15**

10.1 Investment Policy – the Council's investment policy is governed by CLG guidance, which has been implemented in the annual investment strategy approved by the Council on 26/2/2014. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data such as credit rating outlooks and credit default swaps

10.2 The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

10.3 Investments held by the Council - the Council maintained an average balance of £16m of internally managed funds. The internally managed funds earned an average rate of return of 0.58%. The comparable performance indicator is the average 3 month LIBID rate which was 0.47%.

10.4 The investment interest receipts of £145,046 in 2014/15 were in line with the original budget of £100,000.

11.0 **CONCLUSIONS**

11.1 The size of the Council's investment portfolio is relatively small meaning that investment decisions have to be made primarily to accommodate cash flow requirements as opposed to optimising investment returns. Despite these pressures, opportunities for some proactive investment decisions were taken when available.

11.2 During the financial year the Council operated within its approved treasury limits and Prudential Indicators.

12.0 **FINANCIAL IMPLICATIONS/EQUALITY IMPACT ASSESSMENT**

12.1 An Equality Impact Assessment (INRA) is not required.

13.0 **APPENDIX**

Prudential Indicators / Treasury Management Indicators

Background Documents	**Location**	**Contact Officer**
Capita Annual Treasury Management Review Template 2014/15 Finance & Governance Committee TM Strategy January 2014 Statement of Accounts 2014/15 Treasury Register	Room 204 The Grange Ely	Andy Radford Chief Finance officer & S151 Officer (01353) 616269 E-mail: andy.radford@eastcambs.gov.uk

1. PRUDENTIAL INDICATORS	2013/14	2014/15	2014/15
Extract from budget report	**actual**	**original**	**actual**
	£'000	**£'000**	**£'000**
Capital Expenditure			
Non - HRA	£4,273	£1,125	£789
TOTAL	£4,273	£1,125	£789
Ratio of financing costs to net revenue stream			
Non - HRA	(1.62%)	(1.77%)	(%0.9%)
Gross debt	£106	£22	£20
CFR			
Non – HRA	£96	£96	£20
TOTAL	£	£	£
Incremental impact of capital investment decisions	**£ p**	**£ p**	**£ p**
Increase in council tax (band D) per annum	£5.96	£4.08	£2.86

2. TREASURY MANAGEMENT INDICATORS	2013/14	2014/15	2014/15
	actual £'000	original £'000	actual £'000
Authorised Limit for external debt -			
borrowing	£4741	£4894	£4980
other long term liabilities	£259	£106	£20
TOTAL	£5000	£5000	£5000
Operational Boundary for external debt -			
borrowing	£0	£0	£0
other long term liabilities	£259	£106	£20
TOTAL	£	£	£
Actual external debt	£106	£22	£20
Upper limit for fixed interest rate exposure			
Net interest re fixed rate borrowing / investments	£25	£25	£25
Upper limit for variable rate exposure			
Net interest re variable rate borrowing / investments	£25	£25	£25
Upper limit for total principal sums invested for over 364 days (per maturity date)	£2,000	£2,000	£2,000

Maturity structure of fixed rate borrowing during 2014/15	upper limit	lower limit
under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within 5 years	100%	0%
5 years and within 10 years	100%	0%
10 years and within 20 years	100%	0%
20 years and within 30 years	100%	0%
30 years and within 40 years	100%	0%
40 years and within 50 years	100%	0%