Annual Treasury Management Review
2014/15

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1. Introduction

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).

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 27/02/2014)
- a mid-year (minimum) treasury update report (Council 15/10/2014)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

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.

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 Standards & Audit Committee before they were reported to the full Council.

2. The Economy and Interest Rates

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.

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 in May 2015.

3. Overall Treasury Position as at 31 March 2015

The Council's debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through Member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices. At the beginning and the end of 2014/15 the Council's treasury position was as follows:

TABLE 1	31 March 2014 Principal £000	Rate/ Return %	Average Life years	31 March 2015 Principal £000	Rate/ Return %	Average Life years
General Fund:						
Long term debt	**4,298**	**6.21**	**10.1**	**4,097**	**6.13**	**9.5**
CFR	**10,660**			**13,627**		
Over / (under) borrowing	**(6,362)**			**(9,530)**		
Short term debt	**5,060**	**0.39**		**2,000**	**0.35**	
HRA:						
Long term debt	**135,609**	**3.92**	**23.8**	**133,949**	**3.89**	**23.1**
CFR	**140,540**			**138,482**		
Over / (under) borrowing	**(4,931)**			**(4,533)**		
Total investments	**23,122**	**0.34**		**24,162**	**0.96**	
Net debt	**121,845**			**115,884**		

4. The Strategy for 2014/15

The Council's overall core borrowing strategy is as follows:-

- To reduce the revenue costs of debt
- To manage the Council's debt maturity profile, leaving no one future year with a high level of repayments that might cause problems in re-borrowing
- To secure funding at the cheapest cost commensurate with future risk
- To reschedule debt in order to take advantage of potential savings as interest rates change. Any reschedule exercise will be considered in terms of the premiums and discounts on the General Fund and HRA.
- To manage the day to day cash flow of the Authority in order to, where possible, negate the need for short term borrowing.

The Chief Finance Officer will take the most appropriate form of borrowing depending on prevailing interest rates at the time. It is likely that short term fixed rates may provide lower cost opportunities in the short/medium term.

The option of postponing borrowing and running down investment balances will also be considered. This would reduce counterparty risk and offset the expected fall in investment returns.

Change in strategy during the year – the strategy adopted in the original Treasury Management Strategy Report for 2014/15 approved by the Council on 27/02/2014 was subject to revision during the year. Counterparty limits for UK part nationalized banks were increased and specified and non-specified investments previously available only to the external fund managers were extended to be available to the in-house investment team too. These changes were made to provide increased flexibility in terms of the amounts that could be invested and the range of financial instruments available.

5. The Borrowing Requirement and Debt

The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's debt position. The CFR results from the capital activity of the Council and what resources have been used to pay for the capital spend. It represents the 2014/15 and prior years' net or unfinanced capital expenditure that has not yet been charged to revenue or other resources.

Part of the Council's treasury activities is to address the funding requirement for this borrowing need. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board (PWLB) or the money markets), or utilising temporary cash resources within the Council.

The General Fund element of the CFR is reduced each year by a statutory revenue charge.

The total CFR can also be reduced by:

- The application of additional capital financing resources (such as capital receipts); or
- Charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP)

CFR: General Fund	31 March 2014 Actual £000	31 March 2015 Revised £000	31 March 2015 Actual £000
Opening balance	8,357	10,660	10,660
Add unfinanced capital expenditure	2,620	2,485	3,351
Less MRP/VRP	(317)	(384)	(384)
Closing balance	10,660	12,761	13,627

CFR: HRA	31 March 2014 Actual £000	31 March 2015 Revised £000	31 March 2015 Actual £000
Opening balance	142,680	140,540	140,540
Add unfinanced capital expenditure	-	-	50
Less MRP/VRP	(2,140)	(2,108)	(2,108)
Closing balance	140,540	138,432	138,482

6. Borrowing Outturn for 2014/15

Borrowing – There was no new long term borrowing during the year.

Rescheduling - No rescheduling was undertaken during the year.

Repayments – Repayments of £1m were made in the year.

Interest payable on borrowing	2013/14 Actual £000	2014/15 Revised £000	2014/15 Actual £000
General Fund	541	552	522
HRA	5,440	5,183	5,152

7. Investment Outturn for 2014/15

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 27/02/2014. 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 rating outlooks, credit default swaps, bank share prices etc.).

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

Investments held by the Council - the Council maintained an average balance of £8.1m of internally managed funds. The internally managed funds earned an average rate of return of 0.65%. The comparable performance indicator is the average 7-day LIBID rate (uncompounded), which was 0.35%. This compares with a budget assumption of £7.9m investment balances earning an average rate of 0.65%.

Investments held by fund managers – the Council used Investec Asset Management as external fund managers to invest part of its cash balances. The performance of the managers against the benchmark return was:

Fund Manager	Investments Held	Return	Benchmark*
Investec	£21.7m	0.89%	0.37 %

This compares with a budget assumption of average investment balances of £21.7m at 0.8% investment return. Investec announced that they were leaving the local authority market in the first quarter of 2015/16, and all balances were returned to the Council in July 2015.

Appendix 1: Prudential and treasury indicators

1. PRUDENTIAL INDICATORS	2013/14	2014/15	2014/15
Extract from budget and rent setting report	**actual**	**revised**	**actual**
	£'000	**£'000**	**£'000**
Capital Expenditure			
General Fund	6,458	7,933	8,002
HRA	12,739	13,000	15,423
TOTAL	19,197	20,933	23,425
Ratio of financing costs to net revenue stream			
General Fund	4.53%	4.76%	4.50%
HRA	15.31%	13.82%	13.80%
Gross borrowing requirement General Fund			
brought forward 1 April	8,638	9,358	9,358
carried forward 31 March	9,358	6,097	6,097
in year borrowing requirement	720	(3,261)	(3,261)
Gross borrowing requirement HRA			
brought forward 1 April	138,104	135,609	135,609
carried forward 31 March	135,609	133,949	133,949
in year borrowing requirement	(2,495)	(1,660)	(1,660)
Gross debt	144,967	140,535	140,046
CFR			
General Fund	10,660	12,761	13,627
HRA	140,540	138,432	138,482
TOTAL	151,200	151,193	152,109
Annual change in Cap. Financing Requirement			
General Fund	2,303	2,101	2,967
HRA	(2,140)	(2,108)	(2,058)
TOTAL	163	(7)	909

2. TREASURY MANAGEMENT INDICATORS	2013/14	2014/15	2014/15
	actual	**revised**	**actual**
	£'000	**£'000**	**£'000**
Authorised Limit for external debt -			
borrowing	161,500	156,000	156,000
other long term liabilities	-	-	-
TOTAL	161,500	156,000	156,000
Operational Boundary for external debt -			
borrowing	150,250	145,000	145,000
other long term liabilities	-	-	-
TOTAL	150,250	145,000	145,000
Actual external debt	144,967	140,535	140,046
Maximum HRA debt limit	155,612	155,612	155,612
Upper limit for fixed interest rate exposure	50-100%	50-100%	50-100%
Upper limit for variable rate exposure	0-50%	0-50%	0-50%
Upper limit for total principal sums invested for over 364 days (per maturity date)	25%	25%	25%

Maturity structure of fixed rate borrowing during 2014/15	upper limit	lower limit
under 12 months	15%	0%
12 months and within 24 months	15%	0%
24 months and within 5 years	45%	0%
5 years and within 10 years	75%	5%
10 years and above	75%	25%