

NORTH LINCOLNSHIRE COUNCIL

AUDIT COMMITTEE

**TREASURY MANAGEMENT AND INVESTMENT STRATEGY 2016/17
QUARTERLY REPORT**

1. OBJECT AND KEY POINTS IN THIS REPORT

1.1. This is a report on treasury performance to date in 2016/17. The benchmark for measuring performance is the treasury strategy which the council set at its meeting on 23 February 2016.

1.2. The report covers

- The legal and regulatory framework
- The council's strategy
- A review of the current position

1.3. The key points are that the council

Will receive less interest from its investments. Following the 'EU Membership Referendum' vote the base rate was cut to 0.25%

Has an on-going need to borrow to finance its capital programme. The council will undertake Long Term borrowing at the most appropriate point in the year and will manage any cash flow requirements with short term borrowing in the interim.

The Council has accessed the intra-Local Authority lending market as a means of funding its short-term borrowing requirement at well below PWLB rates.

2. BACKGROUND INFORMATION

The legal and regulatory framework

2.1. The annual treasury management and investment strategy was prepared in line with

- CIPFA Code of Practice in the Public Service Fully Revised 2011
 - CIPFA The Prudential Code Fully Revised Second Edition 2011
 - DCLG Guidance
 - Local Government Act 2003
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- 2.2. The code of practice requires that full Council receive a report on treasury management strategy at the start of the financial year, at mid-year and at year end. The Audit Committee receives progress reports at each meeting and an annual report on the outturn position.
- 2.3. It also requires the Council to maintain suitable Treasury Management Practices (TMPs), setting out the manner in which the organisation will seek to achieve its Treasury Management policies and objectives, and prescribing how it will manage and control those activities. As part of this ongoing process the Treasury Management Practices adopted by the Council are reviewed on a regular basis.
- 2.4. No treasury activity is without risk, these include credit risk, liquidity risk, interest rate risk and reputational risk. The Authority has access to data tools that are used to monitor risk and against which decisions on investment and borrowing can be weighed.

3. OPTIONS FOR CONSIDERATION

- 3.1. There are no options for consideration. However the performance against the approved strategy can be evaluated. The annual strategy covers:
- the investment strategy
 - the borrowing strategy
 - and the prudential indicators for external debt and treasury management.

The Strategy for 2016-17

- 3.2. The strategy for 2016/17 was based on the council's views on interest rates and appropriate counterparties for investment and borrowing based on experience, market intelligence including that provided by credit rating agencies, brokers, advisors and the financial press.

The key projections were:

- An average bank base rate of 0.5% (£50k target)
- An average loan rate of 4%

The Investment Strategy

- 3.3. The Investment strategy for 2016-17 aimed to reduce risk by;

- Maintaining a low level of cash balances consistent with ensuring adequate liquidity
- Limiting the maximum investment period to twelve months
- Applying a maximum investment limit of £7m or lower for counter-parties (except the council's own bankers)
- Applying a maximum limit to financial groups rather than separate institutions
- Investing in a range of financial institutions including UK institutions with a minimum of an adequate credit rating or equivalent and Money Market Funds.
- Investing in additional instruments such as Certificates of Deposit

(see **Appendix 1** for list of approved counterparties)

The Borrowing Strategy

3.4. The Borrowing Strategy for 2016-17 aimed to;

- Borrow at the most advantageous point possible
- Track short-and long-term interest rates alongside investment rates to determine that point
- Consider borrowing from a range of institutions to ensure the best value for money
- Generally borrow only to support the capital programme
- Borrow for shorter periods if cash flow requires or to avoid long term borrowing for a period.

Period 8 Review 2016/17

3.5. In economic terms, at the beginning of the period, the risk environment was relatively stable but altered materially following the EU Membership Referendum. The initial stock market shock quickly abated but there will be a period of prolonged uncertainty over the next few years. Markets have adopted a 'wait and see' position towards Brexit negotiations and the new US Administration.

3.6. The key issues of the P8 Treasury Review are:

- Following EU Membership Referendum gilt yields fell markedly and the Governor of the Bank of England pursued a policy of monetary easing resulting in a 0.25% base rate cut and £70bn of Quantitative Easing. Since then gilt yields have recovered.
- At the 30/11/16 the Authority had £121.835m of long term borrowing, £13m of short term borrowing and £2.7m of investments. Short term temporary borrowing ensures that the underlying liquidity need of the authority has been met through-out the period. The most efficient source of funds is the intra-Local Authority market and these have been used to provide flexible and low interest rate borrowing. Details are as shown below:-

NAME	START DATE	AMOUNT	% INTEREST RATE	MATURITY DATE
West Yorkshire Combined Authority	11/04/2016	£ 5,000,000.00	0.35%	22/04/2016
Greater Manchester Combined Authority	23/05/2016	£ 5,000,000.00	0.38%	23/06/2016
Shropshire & Wrekin Fire Authority	23/05/2016	£ 2,000,000.00	0.38%	23/06/2016
Manchester City Council	03/06/2016	£ 3,000,000.00	0.38%	01/07/2016
Greater Manchester Combined Authority	23/06/2016	£ 5,000,000.00	0.38%	25/07/2016
South Yorkshire Combined Authority	23/06/2016	£ 5,000,000.00	0.60%	23/03/2017
Manchester City Council	01/07/2016	£ 3,000,000.00	0.38%	01/08/2016
West Yorkshire Police Commissioners	06/07/2016	£ 3,000,000.00	0.55%	06/02/2017
Vale of Glamorgan Council	06/07/2016	£ 2,000,000.00	0.50%	06/01/2017
Basildon Borough Council	06/07/2016	£ 2,000,000.00	0.47%	07/11/2016
Middlesborough Council	29/09/2016	£ 3,000,000.00	0.20%	06/10/2016
Portsmouth Council	25/11/2016	£ 3,000,000.00	0.36%	02/12/2016

- Investment balances have varied from £15.4m down to £2.7m over the period. Changes to government funding profiles have smoothed the in-year peaks and troughs of recent years. With swings in cash requirement of up to £10m over a few days, to provide assurance that our liquidity needs are met target average balances are maintained c£5m-£10m using the short term loan market.
- Average Return on invested funds during the period was 0.18%. The average rate for 2016/17 so far is 0.29%. This is below target, and reflects the reduction in base rate.
- Some funds were reintroduced to the CCLA Money Market Fund towards the end of the period as market conditions settled following EU referendum and US elections. This fund offers the advantage of diversifications across a range of counterparties more than we could access ourselves directly. However, it is a relatively small fund and has a closed investor base (local authorities only) and so deposits were kept well within the limit of £5m at £2m (around 0.6% of the fund) maximum. Details are as shown below:-

Counterparty Name	Deal Type (+)	Outstanding	Outstanding	Avg Rate	Avg Duration
Barclays Bank plc	Total	£1,913,809	71.68%	0.2000%	0
CCLA The Public Sector Deposit 5 National	Total	£750,000	28.09%	0.2903%	0
Westminster Bank plc	Total	£5,888	0.22%	0.2500%	0
Lloyds Bank plc	Total	£244	0.01%	0.1500%	0
	Total	£2,669,941		0.2255%	0

- The Council has over a period of years eliminated credit risk by using cash reserves instead of long-term external borrowing to support capital investment. In 2015/16 it resumed long-term borrowing and it is expected that there will be a requirement to undertake a sizeable programme of external borrowing over the plan period to support the capital programme, to repay debt and to support reserve drawdown.
- The latest prudential indicator data is shown at **Appendix 2**.

4. ANALYSIS OF OPTIONS

- 4.1 This is a report on past performance and there are no options to consider.
- 4.2 The borrowing decisions made were taken after review of the most appropriate options in terms of value, tenure and fit with our projected short and long terms needs.

5. RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY, IT)

- 5.1 The financial implications to this report are covered in section 3.
 - 5.2 Staff time has been effectively dedicated to the gathering of intelligence and the building up of research capacity to aid, sustain and inform the treasury management function in making borrowing and investment decisions.
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6. **OUTCOMES OF INTEGRATED IMPACT ASSESSMENT (IF APPLICABLE)**

6.1 Not applicable

7. **OUTCOMES OF CONSULTATION AND CONFLICTS OF INTERESTS DECLARED**

7.1 Not applicable

8. **RECOMMENDATIONS**

8.1 That the Audit Committee considers the assurance provided by this report on the effectiveness of arrangements for treasury management, and:

8.2 That the Audit Committee notes the Treasury Management performance to date for the 2016-17 financial year.

DIRECTOR OF POLICY AND RESOURCES

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Background Papers used in the preparation of this report

CIPFA Code of Practice in the Public Service Fully Revised 2011

CIPFA The Prudential Code Fully Revised Second Edition 2011

DCLG Guidance

Local Government Act 2003

COUNTERPARTY LIST

BANKS	Fitch		Moody's		Standard & Poor's		Counterparty Limit
	ST	LT	ST	LT	ST	LT	£
<u>United Kingdom</u>							
Barclays Bank	F1	A	P1	A2	A-2	A	£14,000,000
HSBC Bank plc	F1+	AA-	P1	Aa2	A-1+	AA-	£7,000,000
Santander UK	F1	A	P1	Aa3	A-1	A	£7,000,000
Standard Chartered Bank	F1	A+	P1	Aa3	A-1	A	£7,000,000
<u>Lloyds Banking Group</u>							£7,000,000
Bank of Scotland	F1	A+	P1	A1	A-1	A	
Lloyds Bank	F1	A+	P1	A1	A-1	A	
<u>RBS Group</u>							£4,000,000
National Westminster Bank	F2	BBB+	P2	A3	A-2	BBB+	
Royal Bank of Scotland	F2	BBB+	P2	A3	A-2	BBB+	

BUILDING SOCIETIES	Fitch		Moody's		Standard & Poor's		Counterparty Limit
	ST	LT	ST	LT	ST	LT	£
Nationwide	F1	A	P1	A1	A-1	A	£7,000,000
Coventry	F1	A	P1	A2			£4,000,000
Leeds	F1	A-	P1	A2			£4,000,000
Principality	F2	BBB+	P3	Baa3			£4,000,000
Skipton	F2	BBB+	P2	Baa2			£4,000,000
Yorkshire	F1	A-	P2	A3			£4,000,000

GOVERNMENT INSTITUTIONS							
Debt Management Office							Unlimited
Local authorities							
District Council's							£3,000,000
All Other LA's							£5,000,000
Fire Authorities							£5,000,000
Police authorities							£5,000,000

MONEY MARKET FUND	Fitch	Moody's	Standard & Poor's
Funds rated by at least one agency as:	AAAMmf	Aaa-mf	AAAm

Prudential Indicators

Treasury Management Indicators

The Authority measures and manages its exposures to treasury management risks using the following indicators.

Interest Rate Exposures: This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of net principal borrowed for 2016/19 are:

	2016/17	2017/18	2018/19
Upper % limit on fixed interest rate exposure	100%	100%	100%
Actual	86%	-	-
Upper % limit on variable interest rate exposure	20%	20%	20%
Actual %	14%	-	-

Maturities falling within 12 months are classed as 'variable rate' as they are exposed to short-term rate fluctuations should they need to be replaced on maturity.

Maturity Structure of Borrowing: This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing for 2016/17 are:

	Upper	Lower	Actual
Under 12 months	20%	0%	14%
12 months and within 24 months	15%	0%	5%
24 months and within 5 years	50%	0%	3%
5 years and within 10 years	75%	0%	22%
Over 10 years	90%	25%	56%

Principal Sums Invested for Periods Longer than 365 days: The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by needing to seek early repayment of its investments. This could occur as a result of a credit event or a change in cash flow circumstances. The council did not invest for longer than 365 days during the period.

Other Prudential Indicators

The following three prudential indicators are relevant to the treasury function as they concern limits on borrowing and the adoption of the CIPFA Treasury Management Code.

Operational Boundary for External Debt: The operational boundary is based on the Authority's estimate of most likely, i.e. prudent, but not worst case scenario for external debt.

Operational Boundary	2016/17 £m	2017/18 £m	2018/19 £m
Borrowing	£205m	£202m	£196m
Other long-term liabilities	£2m	£2m	£2m
Total Debt	£207m	£204m	£198m

Authorised Limit for External Debt: The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Authority can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

Authorised Limit	2016/17 £m	2017/18 £m	2018/19 £m
Borrowing	£257m	£254m	£247m
Other long-term liabilities	£5m	£5m	£5m
Total Debt	£262m	£259m	£252m

Adoption of the CIPFA Treasury Management Code: The Authority adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition in February 2012.

Other Matters

All Treasury Activity is now undertaken through the joint service with North East Lincolnshire Council. Now that the final structure and new systems and process introduced the Treasury Management Practices (TMP's) are being updated to reflect the new arrangements.