ITEM NO. 11.1

Report of:	Head of Finance
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Portfolio Leader:	Leader of the Council
Key Decision:	No
Report Track:	Audit & Governance Cttee. 28/06/16 and Council 06/07/16

COUNCIL

6 JULY 2016

ANNUAL TREASURY MANAGEMENT REPORT 2015/16

1 Purpose of Report

1.1 To update Members on treasury management activity and performance during the 2015/16 financial year.

2 Recommendations

2.1 To note the annual treasury management report for 2015/16

2.2 To approve the actual 2015/16 prudential and treasury indicators as set out in Appendix 1.

3 Key Issues and Reasons for Recommendation

3.1 Treasury management activity and performance during the 2015/16 financial year.

4 Relationship to Corporate Priorities

4.1 Treasury management and investment activity link in with all of the Council's priorities and spending plans.

5 Report Detail

Background

5.1 The 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 2015/16. 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).

5.2 During 2015/16 the minimum reporting requirements were that the full Council should receive the following reports:-

- an annual treasury strategy in advance of the year (Council – 11 February 2015);
- a mid year treasury update report (Council - 13 January 2016);
- an annual review following the end of the year describing the activity compared to the strategy (this report).

5.3 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.

5.4 The Council has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit and Governance Committee before they were reported to the full Council.

The Economy and Interest Rates

5.5 Market expectations for the first increase in Bank Rate moved considerably during 2015/16 due to many fears including concerns that China's economic growth could be heading towards a hard landing; the potential destabilisation of some emerging market countries particularly exposed to the Chinese economic slowdown; and the continuation of the collapse in oil prices during 2015 together with continuing Eurozone growth uncertainties.

5.6 These concerns have caused sharp market volatility in equity prices during the year with corresponding impacts on bond prices and bond yields due to safe haven flows. Bank Rate, therefore, remained unchanged at 0.5% for the seventh successive year. Economic growth (GDP) in 2015/16 has been disappointing with growth falling steadily from an annual rate of 2.9% in quarter 1 2015 to 2.1% in quarter 4.

5.7 The sharp volatility in equity markets during the year was reflected in sharp volatility in bond yields. However, the overall dominant trend in bond yields since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have repeatedly been revised downwards and expectations of increases in central rates have been pushed back. In addition, a notable trend in the year was that several central banks introduced negative interest rates as a measure to stimulate the creation of credit and hence economic growth.

5.8 The ECB commenced a full blown quantitative easing programme of purchases of Eurozone government and other bonds starting in March at €60bn per month. This put downward pressure on Eurozone bond yields. There was a further increase in this programme of QE in December 2015.

5.9 As for America, the economy has continued to grow healthily on the back of resilient consumer demand. The first increase in the central rate occurred in December 2015 since when there has been a return to caution as to the speed of further increases due to concerns around the risks to world growth.

5.10 The UK elected a majority Conservative Government in May 2015, removing one potential concern but introducing another due to the promise of a referendum on the UK remaining part of the EU.

5.11 As members are aware, the UK voted to leave the EU on Thursday 23 June resulting in two of the credit rating agencies downgrading the UK Sovereign rating, reflecting their view that the ‘leave’ result will weaken the stability of the UK economy. Market volatility is expected to continue owing to uncertainty around Brexit.

Overall Treasury Position as at 31 March 2016

5.12 At the beginning and the end of 2015/16 the Council‘s treasury position was as follows:

TABLE 1	31 March 2015 Principal	Rate/ Return	Average Life yrs	31 March 2016 Principal	Rate/ Return	Average Life yrs
Total debt (PWLB)	£85.8m	4.14%	28.1	£85.0m	4.15%	30.0
CFR	£97.1m	-	-	£96.4m	-	-
Over / (under) borrowing	(£11.3m)	-	-	(£11.4m)	-	-
Total investments	£11.7m	0.75%	0.57	£12.4m	0.65%	0.34
Net debt	£74.1m	-	-	£72.6m	-	-

Strategy for 2015/16

5.13 The expectation for interest rates within the treasury management strategy for 2015/16 anticipated low but rising Bank Rate and gradual rises in medium and longer term fixed borrowing rates during 2016/17. 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.

5.14 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.

5.15 The sharp volatility in equity markets during the year was reflected in sharp volatility in bond yields. However, the overall dominant trend in bond yields since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have repeatedly been revised downwards and expectations of increases in central rates have been pushed back.

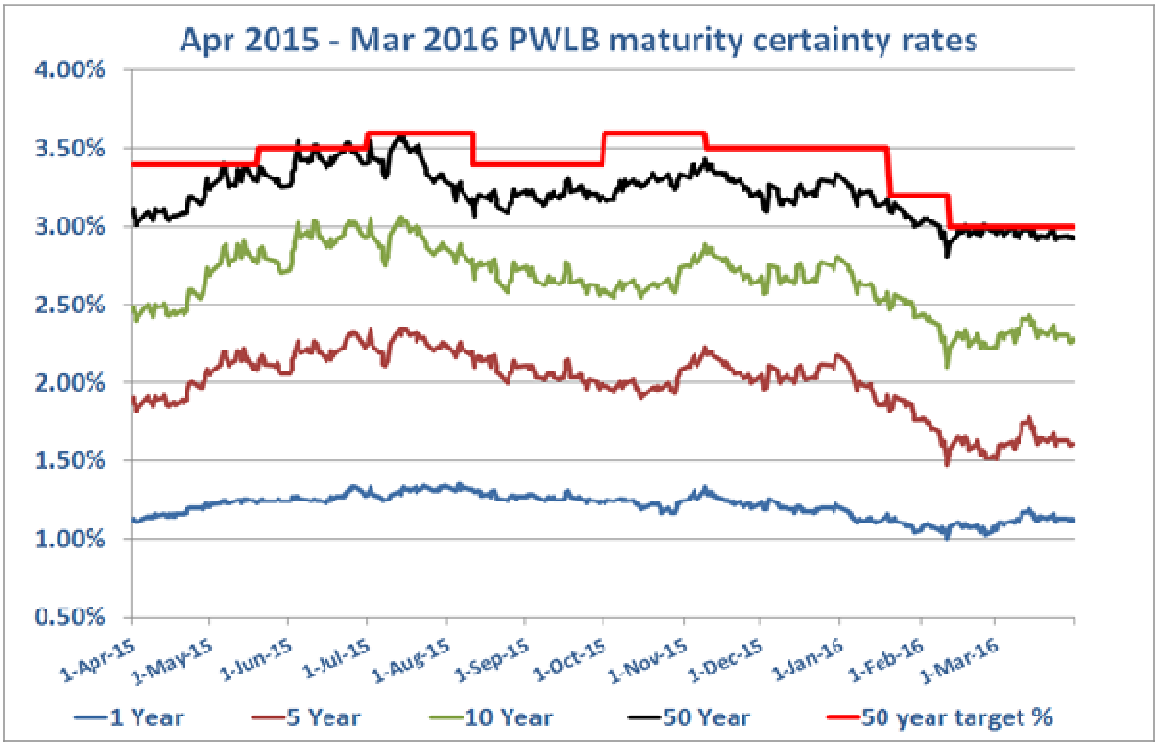
Borrowing Requirement

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

	31 March 2015 Actual	31 March 2016 Budget	31 March 2016 Actual
Capital Financing Requirement	**£97.074m**	**£96.582m**	**£96.419m**

Borrowing Rates in 2015/16

5.17 **PWLB borrowing rates** - the graph below shows how PWLB certainty rates have fallen to historically very low levels during the year.

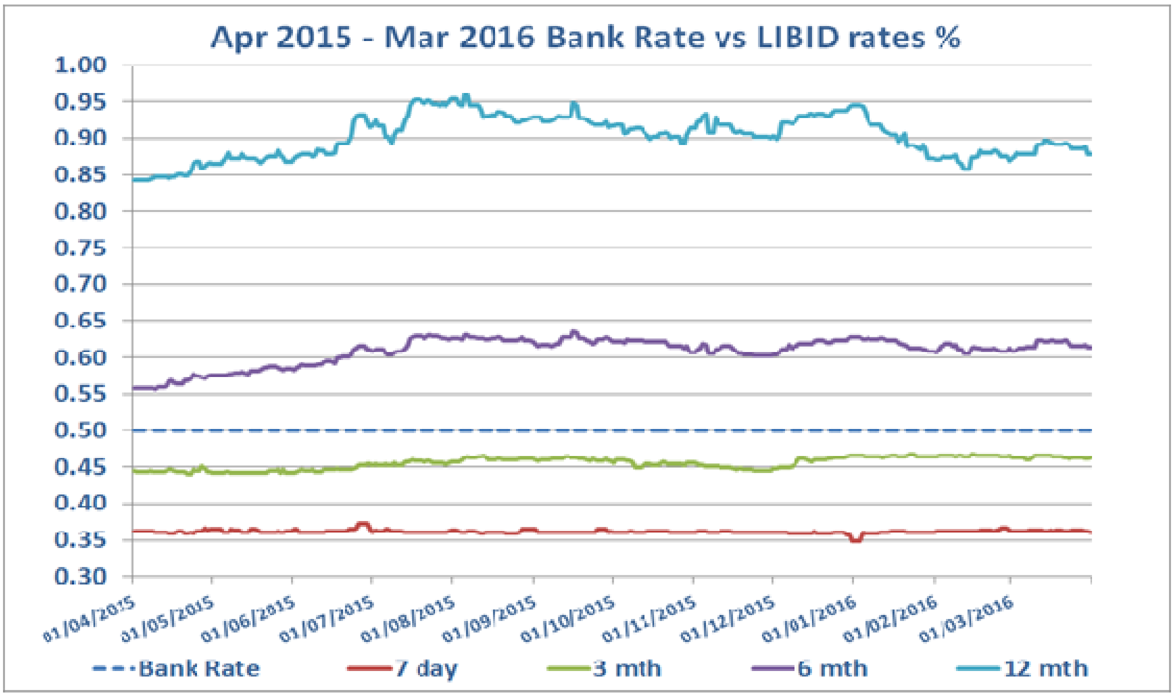


Borrowing Outturn for 2015/16

5.18 **Borrowing** – Due to investment concerns, both counterparty risk and low investment returns, no borrowing was undertaken during the year.

Investment Rates in 2015/16

5.19 Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for seven years. Market expectations as to the timing of the start of monetary tightening started the year at quarter 1 2016 but then moved back to around quarter 2 2018 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 and due to the continuing weak expectations as to when Bank Rate would start rising.



Investment Outturn for 2015/16

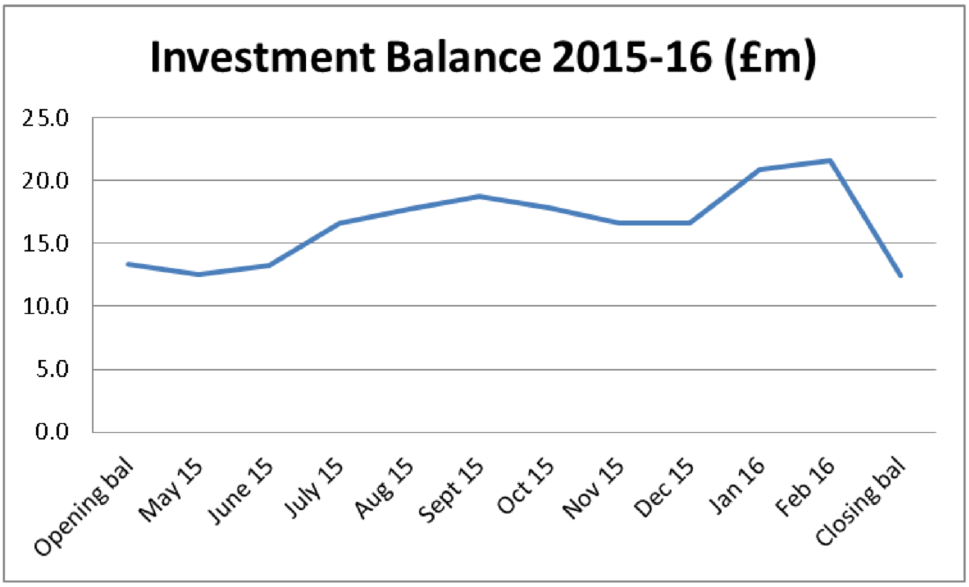
5.20 **Investment Policy** - the Council's investment policy is governed by CLG guidance, which was been implemented in the annual investment strategy approved by the Council on 11 February 2015. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

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

5.22 **Investments as at 31 March 2016** -The Council's investments as at 31 March 2016 are set out in the table below:

Counterparty	Start Date	Maturity	Value (£)	Rate
Natwest Bank plc	Call		461,000	0.25%
Standard Life (MMF)	Call		1,200,000	0.51%
Santander	95 day notice account		5,000,000	0.90%
Credit Suisse	01/10/15	01/04/16	1,000,000	0.68%
Nationwide Building Society	07/01/16	07/07/16	2,000,000	0.71%
Bank of Scotland plc	03/03/16	02/09/16	2,724,000	0.75%
TOTAL			**12,385,000**	**0.65%**

5.23 The chart below illustrates the movement in the level of investments held by the Council at each month end during the year. The peak in year was **£24.5 million** and the average balance for the year was **£18.4 million**.



5.24 The funds earned an average rate of return for the year of **0.65%**. The comparable performance indicator is the average 3 month London Interbank rate (LIBID), which was **0.46%**. The Council's performance exceeds the benchmark by some margin and is a reflection of the success of the strategy of investing a high proportion of the portfolio with UK and European banks offering good rates for fixed term deposits of 6 months and one year.

5.25 Overall investment earnings for the year totalled **£199,000**.

6 Implications

6.1 Financial

The financial implications have been referred to throughout the report.

6.2 **Legal**

The legal implications have been referred to throughout the report.

6.3 **Human Resources**

There are no human resource implications arising from this report.

6.4 **Section 17 (Crime Prevention)**

There are no implications arising from this report.

6.5 **Human Rights Act**

There are no identified implications in respect of the Human Rights Act 1998 arising from this report.

6.6 **Data Protection**

There are no implications arising from this report.

6.7 **Risk Management**

Treasury management is a high risk area due to the large amounts of money dealt with on a daily basis. However, the Council has a Treasury Policy and Strategy in place which is approved each year for the following 12 months. The Council also has advice on investment and lending from the leading company in the field and has instituted a strict control and delegation of duties regime which reduces risk to a minimum.

6.8 **Equality & Diversity**

There are no identified implications arising form this report.

6.9 **Best Value**

The strategy ensures that best value is provided to the Council.

7 Appendices to the Report

Appendix 1	2015-16 Prudential and Treasury Indicators

Previous Consideration

None

Background Papers

Available in Financial Services.

ITEM NO. 11.8

Appendix 1

1. PRUDENTIAL INDICATORS	2014/15	2015/16	2015/16
	actual	estimate	actual
	£'000	£'000	£'000
Capital Expenditure	12,438	22,071	17,335
Ratio of financing costs to net revenue stream (GF)	4.1%	4.3%	3.2%
Gross debt	85,805	85,005	85,005
Capital Financing Requirement as at 31 March	97,074	96,582	96,419
2. TREASURY MANAGEMENT INDICATORS			
Authorised Limit for external debt -	105,605	108,082	108,082
Operational Boundary for external debt	100,355	96,582	96,582
Actual external debt	85,805	85,005	85,005
Upper limit for fixed interest rate exposure	100%	100%	100%
Upper limit for variable rate exposure	75%	75%	75%
Upper limit for total principal sums invested for over 364 days	£10 million	£10 million	£10 million

Maturity structure of fixed rate borrowing during 2015/16	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 above	100%	0%