

Treasury Management Performance to September 2015

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Purpose of Report

1. To review the treasury management activity and the performance against the Prudential Indicators for the six months ended 30th September 2015. To carry out the mid-year review of the Treasury Management Strategy.

Recommendations

2. The Audit Committee are asked to:
 - Note the Treasury Management Activity for the six-month period ended 30th September 2015.
 - Note the position of the individual prudential indicators for the six-month period ended 30th September 2015.
 - Note that we are Increasing our investment with the CCLA Property fund by £1million.
 - review the attached Treasury Management Policy and recommend it to Council (Appendix B)
 - Carry out the mid-year review of the Treasury Management Strategy and recommend it to Council. (Strategy attached with the amendments highlighted – Appendix C)

The Investment Strategy for 2015/16

3. The Council's treasury management activity is underpinned by CIPFA's Code of Practice on Treasury Management ("the Code"), which requires local authorities to produce annually Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity. The Code also recommends that members are informed of treasury management activities at least twice a year. The Council reports six monthly to Full Council against the strategy approved for the year. The scrutiny of treasury management policy, strategy and activity is delegated to the Audit Committee.
4. Treasury management in this context is defined as:

"The management of the local authority's cash flows, its borrowings and its investments, the management of the associated risks, and the pursuit of the optimum performance or return consistent with those risks".
5. The Authority has invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Authority's treasury management strategy.
6. Overall responsibility for treasury management remains with the Council. No treasury management activity is without risk; the effective identification and management of risk are integral to the Council's treasury management objectives.

7. In order to diversify the authority's investment portfolio which is largely invested in cash, investments will be placed with a range of approved investment counterparties in order to achieve a diversified portfolio of prudent counterparties, investment periods and rates of return. Given the increasing risk and continued low returns from short-term unsecured bank investments, the Authority aims to further diversify into more secure and higher yielding asset classes during 2015/16. Maximum investment levels with each counterparty will be set to ensure prudent diversification is achieved

Interest Rates 2015/16

8. Base rate began the financial year and remains at 0.5%.
9. Our advisors are forecasting that the outlook is for official interest rates to remain at 0.5% until June 2016, as shown below:

	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Average
Official Bank Rate														
Upside risk		0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.33
Arlingclose Central Case	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.75	1.75	1.75	1.17
Downside risk				-0.25	-0.50	-0.50	-0.75	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-0.73

Investment Portfolio

10. The table below shows the Council's overall investments as at 30th September 2015:

	Value of Investments at 01.04.15 £	Value of Investments at 30.09.15 £	Fixed/ Variable Rate
Investments advised by Arlingclose			
Money Market Fund (Variable Net Asset Value)	1,001,247	1,001,247	Variable
Property Fund	3,363,303	3,363,303	Variable
Total	4,364,550	4,364,550	
Internal Investments			
Certificates of Deposit	4,512,371	7,000,861	Fixed
Corporate Bonds	11,271,639	12,343,862	Fixed
Floating Rate Notes (FRNs)	9,972,584	10,358,900	Variable
Short Term Deposits (Banks)	7,500,000	19,400,000	Variable
Short Term Deposits (Other LAs)	8,000,000	3,000,000	Variable
Money Market Funds (Constant Net Asset Value) & Business Reserve Accounts	3,720,000	1,310,000	Variable
Total	44,976,594	53,413,623	
TOTAL INVESTMENTS	49,341,144	57,778,173	

Returns for 2015/16

11. The returns to 30th September 2015 are shown in the table below:

	Actual Income £'000	% Rate of Return
Investments advised by Arlingclose		
Payden Money Market Fund (VNAV)	4	
Property Fund (CCLA)	86	
Total	<u>90</u>	4.48
Internal Investments		
Certificates of Deposit (CD's)	19	
Corporate Bonds	77	
Floating Rate Notes (FRNs)	36	
Fixed Term Deposits/T Bills	57	
Money Market Funds (CNAV) & Business	11	
Reserve Accounts		
Total	<u>200</u>	0.75
Other Interest		
Miscellaneous Loans	2	
Total	<u>2</u>	
TOTAL INCOME TO 30TH SEPTEMBER 2015	<u><u>292</u></u>	1.01
PROFILED BUDGETED INCOME	<u><u>231</u></u>	
FORECAST SURPLUS FOR YEAR END	88	

12. The table above shows investment income for the year to date compared to the profiled budget. The annual budget is set at £461,320. We currently estimate that the position at the end of the financial year will be an overall favourable variance in the order of £88,025. This is assuming SSDC receive a dividend of 3p per unit each quarter for its investment in the property fund, however if there is a dip in the economy this could affect the forecasted return.

13. The outturn position is affected by both the amount of cash we have available to invest and the interest base rate set by the Bank of England. Balances are affected by the timing of capital expenditure and the collection of council tax and business rates.

Investments

14. Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2014/15. New investments can be made with the following institutions:

- Other Local Authorities;
- AAA-rated Money Market Funds;

- Certificates of Deposit (CDs) and Term Deposits with UK Banks and Building Societies systemically important to the UK banking system and deposits with select non-UK Banks (Australian, Canadian and American);
- T-Bills and DMADF (Debt Management Office);
- Bonds issued by Multilateral Development Banks, such as the European Investment Bank;
- Commercial Paper
- Other Money Market Funds and Collective Investment Schemes meeting the criteria in SI 2004 No 534, SI 2007 No 573 and subsequent amendments.

15. The graph shown in Appendix A shows the performance of the in-house Treasury team in respect of all investments for the quarter ending 30th September 2015 in comparison to all other clients of Arlingclose.

16. The graph shows that SSDC is in a satisfactory position in terms of the risk taken against the return on investments.

Borrowing

17. An actual overall borrowing requirement (CFR) of £9.7 million was identified at the beginning of 2014/15. As interest rates on borrowing exceed those on investments the Council has used its capital receipts to fund capital expenditure. As at 30th September 2015 the Council had no external borrowing.

Breakdown of investments as at 30th September 2015

Date Lent	Counterparty	Amount	Rate	Maturity Date
5 May 15	Lancashire County Council	1,000,000	0.50	5 Nov 15
6 Jan 14	Greater London Authority	2,000,000	1.03	6 Oct 15
5 May 15	DBS Bank Ltd	2,000,000	0.58	5 Nov 15
26 May 15	Rabobank International	1,000,000	0.58	26 Nov 15
4 Sep 15	Barclays Bank Plc	1,000,000	0.54	11 Dec 15
11 Sep 15	IPA SCB TD Incoming (Santander)	1,000,000	0.65	11 Mar 16
9 Sep 15	United Overseas Bank Ltd	2,000,000	0.60	9 Mar 16
3 Jul 15	Barclays Bank Plc	1,000,000	0.53	9 Oct 15
17 Jul 15	Bank of Scotland	1,000,000	0.57	23 Oct 15
28 Aug 15	Bank of Scotland	1,000,000	1.00	30 Aug 16
30 Sep 15	Nationwide Building Society	1,000,000	0.65	21 Mar 16
15 Jul 15	Toronto Dominion Bank	2,000,000	0.54	15 Jan 16
15 Jul 15	Nationwide Building Society	1,000,000	0.50	19 Oct 15
28 Aug 15	Commonwealth Bank of Australia	1,400,000	0.65	29 Feb 16
7 Sep 15	Coventry Building Society	2,000,000	0.41	7 Oct 15
16 Sep 15	Goldman Sachs International Bank	2,000,000	0.48	18 Dec 15

	Corporate Bonds/Eurobonds			
10 Dec 13	GE Capital UK Funding	1,038,020	1.42	18 Jan 16
17 Jan 14	Places for People Capital Markets	603,877	2.67	27 Dec 16
17 Jan 14	Places for People Capital Markets	459,287	2.67	27 Dec 16
7 Apr 14	Commonwealth Bank of Australia	517,020	1.00	14 Dec 15
8 Apr 14	Nordea Bank AB	515,835	0.98	15 Dec 15
4 Aug 14	Leeds Building Society (Covered)	560,713	2.13	17 Dec 18
22 Oct 14	Yorkshire Building Society (Covered)	1,729,543	1.56	12 Apr 18
5 Mar 15	Volkswagen International Finance	1,015,107	0.70	23 Oct 15
5 Mar 15	Westpac Banking Corporation	1,007,119	0.74	23 Dec 15
17 Apr 15	Heathrow Funding Ltd	1,109,810	0.85	31 Mar 16
7 May 15	Daimler AG	501,440	0.88	10 Dec 15
5 Jun 15	European Investment Bank	2,105,188	0.66	7 Sep 16
12 Jun 15	Prudential Plc	155,191	0.96	16 Nov 15
3 Aug 15	Bank Nederlandse Gemeenten	1,025,712	0.68	26 Feb 16
	Certificates of Deposit (CDs)			
29 Apr 15	Standard Chartered	1,000,150	0.68	29 Oct 15
6 May 15	Nordea Bank AB	500,075	0.56	6 Nov 15
31 Jul 15	Landesbank Hessen-Thuringen	2,000,298	0.69	29 Jan 16
5 Aug 15	Credit Suisse AG London	500,038	0.50	5 Nov 15
7 Aug 15	Standard Chartered	1,000,149	0.70	5 Feb 16
26 Aug 15	Oversea Chinese Banking Corporation	2,000,151	0.50	26 Nov 15
	Floating Rate Notes (FRNs)			
25 Nov 13	HSBC Bank PLC	1,004,169	0.82	16 May 16
3 Apr 14	Yorkshire Building Society *Covered*	1,005,441	0.98	23 Mar 16
22 Oct 14	Abbey National Treasury Services *Covered*	1,034,829	0.71	5 Apr 17
21 Nov 14	Barclays Bank Plc *Covered*	1,000,341	0.68	15 Sep 17
25 Mar 15	Lloyds Bank Plc *Covered*	2,006,200	0.64	16 Jan 17
29 Apr 15	Toronto Dominion *Covered*	1,002,572	0.66	20 Nov 17
26 Jun 15	Nationwide Building Society *Covered*	1,001,774	0.68	17 Jul 17
2 Jul 15	National Australia bank Ltd	1,503,339	0.67	12 Aug 16
10 Sep 15	Cooperative Centrale Raiffeisen Boerenleenbank	800,235	0.49	23 Oct 15
	Pooled Funds & Money Market Funds			
	Payden Fund VNAV	1,001,247	0.88	
	CCLA Property Fund	3,363,303	5.68	
	Federated Money Market Fund	500,000	0.39	
	Blackrock Money Market Fund	810,000	0.44	
	TOTAL	55,474,599		

* Note: Money Market Funds are instant access accounts so the rate displayed is a daily rate

Prudential Indicators – Quarter 2 monitoring

Background:

18. In February 2015, Full Council approved the indicators for 2015/16, as required by the Prudential Code for Capital Finance in Local Authorities. The Local Government Act 2003 allowed local authorities to determine their own borrowing limits provided they are affordable and that every local authority complies with the code.

Prudential Indicator 1 - Capital Expenditure:

19. The revised estimates of capital expenditure to be incurred for the current year compared to the original estimates are:

	2015/16 Original Estimate £'000	Expected Outturn £'000	2015/16 Variance £'000	Reason for Variance
Approved capital schemes	5,568	4,450	(1,118)	Re-profiling of the expenditure to future years
Reserves	404	1,634	1,230	Slippage from 2014/15 into 2015/16
Total Expenditure	5,972	6,084	112	

20. The above table shows that the overall estimate for capital expenditure has increased.

Prudential Indicator 2 - Ratio of Financing Costs to Net Revenue Stream:

21. A comparison needs to be made of financing capital costs compared to the revenue income stream to support these costs. This shows how much of the revenue budget is committed to the servicing of finance.

Portfolio	2015/16 Revised Estimate £'000	Expected Outturn £'000	2015/16 Variance £'000	Reason for Variance
Financing Costs*	(338)	(402)	(64)	Better return on the Property fund is expected but this is dependent on the economy
Net Revenue Stream	17,390	17,741	351	Carry forwards approved of £303k and £44k contribution from the Somerset Rivers Authority
%*	(1.9)	(2.3)		

*figures in brackets denote income through receipts and reserves

22. The financing costs include interest payable, notional amounts set aside to repay debt, less, interest on investment income. The figure in brackets is due to investment income outweighing financing costs significantly for SSDC but is nevertheless relevant since it shows the extent to which the Council is dependent on investment income.

Prudential Indicator 3 - Capital Financing Requirement:

23. The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. Estimates of the year-end capital financing requirement for the authority are:

	2015/16 Original Estimate £'000	Expected Outturn £'000	2015/16 Variance £'000	Reason for Variance
Opening CFR	9,484	9,447	(37)	
Capital Expenditure	5,192	5,991	799	See explanation for Prudential Indicator 1 above
Capital Receipts*	(5,046)	(4,450)	596	
Grants/Contributions*	(146)	(1,541)	(1,395)	
Minimum Revenue Position (MRP)	(123)	(148)	(25)	One lease has been amended to be repaid over a shorter period hence an increase in the current years MRP
Closing CFR	9,361	9,299	(62)	

*Figures in brackets denote income through receipts or reserves.

Prudential Indicator 4 – Gross Debt and the Capital Financing Requirement:

24. The Council is also required to ensure that any medium term borrowing is only used to finance capital and therefore it has to demonstrate that the gross external borrowing does not, except in the short term exceed the total of capital financing requirements over a three year period. This is a key indicator of prudence.

	2015/16 Original Estimate £'000	2015/16 Qtr 2 Actual £'000	2015/16 Variance £'000	Reason for Variance
Borrowing	0	0	0	
Finance Leases	248	186	(62)	Amendment to the MRP has reduced the amount outstanding on the finance leases
Total Debt	248	186	(62)	

25. Total debt is expected to remain below the CFR.

Prudential Indicator 5 - Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure:

26. The Council must set three years of upper limits to its exposure to the effects of changes in interest rates. As a safeguard, it must ensure that its limit would allow it to have up to 100% invested in variable rate investments to cover against market fluctuations. For this purpose, term deposits of less than 365 days are deemed to be

variable rate deposits. Fixed rate deposits are investments in Eurobonds, Corporate Bonds and term deposits exceeding 365 days.

	2015/16 % Limit	2015/16 Qtr 2 Actual %	2015/16 Variance %	Reason for Variance
Fixed	80	5.29	(74.71)	Within limit
Variable	100	94.71	(5.29)	Within limit

27. The Council must also set limits to reflect any borrowing we may undertake.

	2015/16 % Limit	2015/16 Qtr 2 Actual %	2015/16 Variance %	Reason for Variance
Fixed	100	0	100	SSDC currently has no borrowing
Variable	100	0	100	SSDC currently has no borrowing

28. The indicator has been set at 100% to maximise opportunities for future debt as they arise.

Prudential Indicator 6 - Upper Limit for total principal sums invested over 364 days:

29. SSDC must also set upper limits for any investments of longer than 364 days. The purpose of this indicator is to ensure that SSDC, at any time, has sufficient liquidity to meet all of its financial commitments.

Upper Limit for total principal sums invested over 364 days	2015/16 Maximum Limit £'000	2015/16 Qtr 2 Actual (Principal amount) £'000	Reason for Variance
Between 1-2 years	25,000	6,000	Within limit
Between 2-3 years	20,000	2,500	Within limit
Between 3-4 years	10,000	500	Within limit
Between 4-5 years	10,000	0	Within limit
Over 5 years	5,000	0	Within limit

30. The table above shows that the Council adopts a policy of safeguarding its investments by minimising investments that are redeemable more than five years ahead.

Prudential Indicator 7 – Credit Risk:

31. The Council considers security, liquidity and yield, in that order, when making investment decisions.

Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the Council's assessment of counterparty credit risk.

The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution and its sovereign
- Sovereign support mechanisms
- Credit default swaps (where quoted)
- Share prices (where available)
- Economic Fundamentals, such as a country's net debt as a percentage of its GDP
- Corporate developments, news articles, markets sentiment and momentum
- Subjective overlay

The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

Prudential Indicator 8 - Actual External Debt:

32. This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities (this represents our finance leases). This Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

Actual External Debt as at 31/03/2015	£'000
Borrowing	0
Liabilities arising from finance leases	334
Total	334

Prudential Indicator 9 - Authorised Limit for External Debt:

33. The Council has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy. Borrowing will arise as a consequence of all the financial transactions of the Council not just arising from capital spending.
34. This limit represents the maximum amount that SSDC may borrow at any point in time during the year. If this limit is exceeded the Council will have acted ultra vires. It also gives the Council the responsibility for limiting spend over and above the agreed capital programme. A ceiling of £12 million was set to allow flexibility to support new capital projects over and above the identified borrowing requirement.

	2015/16 Estimate £'000	2015/16 Qtr 2 Actual £'000	2015/16 Variance £'000	Reason for Variance
Borrowing	11,000	0	(11,000)	SSDC currently has no external borrowing
Other Long-term Liabilities (Finance Leases)	1,000	186	(814)	Within limit
Total	12,000	186	(11,814)	

Prudential Indicator 10 – Operational Boundary for External Debt:

35. The operational boundary sets the limit for short term borrowing requirements for cash flow and has to be lower than the previous indicator, the authorised limit for external debt. A ceiling of £10 million was set.

	2015/16 Estimate £'000	2015/16 Qtr 2 Actual £'000	2015/16 Variance £'000	Reason for Variance
Borrowing	9,200	0	(9,200)	SSDC currently has no external borrowing
Other Long-term Liabilities (Finance Leases)	800	186	(614)	Within limit
Total	10,000	186	(9,814)	

Prudential Indicator 11 - Maturity Structure of Fixed Rate borrowing:

36. This indicator is relevant to highlight the existence of any large concentrations of fixed rated debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest changes in any one period. When we borrow we can take a portfolio approach to borrowing in order to reduce interest rate risk. This indicator is shown as the Council has set limits in anticipation of future borrowing.

Maturity structure of fixed rate borrowing	2014/15 Actual %	2015/16 Qtr 1 Actual %	Lower Limit %	Upper Limit %
Under 12 months	0	0	0	100
12 months and within 24 months	0	0	0	100
24 months and within 5 years	0	0	0	100
5 years and within 10 years	0	0	0	100
10 years and within 20 years	0	0	0	100
20 years and within 30 years	0	0	0	100
30 years and within 40 years	0	0	0	100
40 years and within 50 years	0	0	0	100
50 years and above	0	0	0	100

As the council doesn't have any fixed rate external borrowing at present the above upper and lower limits have been set to allow flexibility.

Prudential Indicator 12 - Incremental Impact of Capital Investment Decisions:

37. SSDC must show the effect of its annual capital decisions for new capital schemes on the council taxpayer. Capital spend at SSDC is financed from additional receipts so the figure below actually shows the possible decreases in council tax if all capital receipts were invested rather than used for capital expenditure.

Incremental Impact of Capital Investment Decisions	2015/16 Estimate £	2016/17 Estimate £	2017/18 Estimate £
Decrease in Band D Council Tax	0.07	0.17	0.17

Prudential Indicator 13 - Adoption of the CIPFA Treasury Management Code:

38. This indicator demonstrates that the Council has adopted the principles of best practice.

Adoption of the CIPFA Code of Practice in Treasury Management
The Council approved the adoption of the CIPFA Treasury Management Code at its Council meeting on 18 th April 2002.

Conclusion

39. The council is currently within all of the Prudential Indicators and is not forecast to exceed them.

Background Papers: Prudential Indicators Working Paper, Treasury Management Strategy Statement 2015/16, Quarter 2 2015/16 Capital Programme.

Appendix A

