



Peter McCall

Treasury Management Activities 2016/17 Quarter 4 (January to March 2016) and Annual Report 2016/17

PCC Decision Meeting 10 May 2017 and JASC Meeting 24 May 2017

Purpose of the Report

The purpose of this paper is to report on the Treasury Management Activities (TMA), which have taken place during the period January to March 2017, in accordance with the requirements of CIPFA's Code of Practice on Treasury Management.

TMA are undertaken in accordance with the Treasury Management Strategy Statement (TMSS) and Treasury Management Practices (TMPs) approved by the Commissioner in February each year.

Recommendations

The Commissioner is asked to note the contents of this report.

JASC Members are asked to note the contents of this report. The report is provided as part of the arrangements to ensure members are briefed on Treasury Management and maintain an understanding of activity in support of their review of the annual strategy.

Economic Background

Financial uncertainty post Brexit and the USA election resulted in market volatility during 2016/17. The Bank of England (BOE) Base Rate was reduced from 0.50% to **0.25%** on 4 August 2016. Quantitative Easing (QE) was increased from £375bn to **£435bn** on the same date.

The treasury advisor's Arlingclose central case is for the Bank Base Interest Rate to remain at 0.25%, but there is a low possibility of a drop to close to zero, with a very small chance of a reduction below zero.

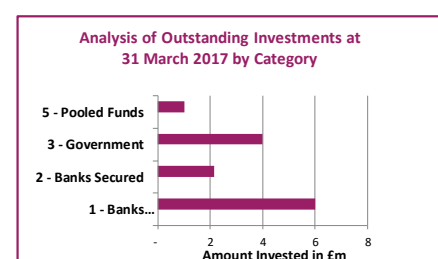
Consumer Price Index (CPI) inflation was subdued for the first part of the year but the sharp fall in the sterling exchange rate post Brexit and rising energy prices resulted in CPI rising from 0.3% year on year in April 2016 to 2.3% year on year in March 2017. According to the ONS, CPI will be heading close towards the Bank of England's target rate of 2% in the first half of 2017, consistent with the forecasts contained within the Bank's last quarterly Inflation Report issued in February 2017.

TM Operations and Performance Measures

The Commissioners day to day TMA are undertaken in accordance with the TMSS. The TMSS establishes an investment strategy with limits for particular categories of investment and individual counterparty limits within the categories.

Outstanding Investments: As at 31 March 2017 the total value of investments was **£13.155m** and all were within TMSS limits.

The chart below shows the outstanding investments at 31 March by category.



A full list of the investments that make up the balance of £13.155m is provided at **Appendix A**.

Investment Activity: During quarter 4 a total of 3 investments with a combined value of £4m were made within TM categories 1-3 (banks unsecured, banks secured and Government). In addition to these there were regular smaller investments in category 5 (money market pooled funds).

Non-specified investments: The TMSS sets a limit for investments with a duration of greater than 364 days at the time the investment is made (known as non-specified investments), this limit is £5m. At 31 March the Commissioner had two investments meeting this description with a combined total of £4.2m. Of these two, only 1 has an outstanding duration of over 364 days. These investments are:

- Leeds Building Society £2.2m 887 days (13/07/16 to 17/12/18)
- Lloyds Bank £2m 366 days (11/08/16 to 11/08/17)

Investment Income: The budget for investment interest receivable in 2016/17 was £100k. The actual income achieved against this target was £102k which provides a slight excess of £2k (2%). Previous reports forecast a shortfall of £10k, this position was recovered as a result of investments secured earlier in the

year at higher rates and the rates not falling as quickly as expected.

The average return on investment at the end of quarter 4 is 0.38%. As a measure of investment performance the rate achieved on maturing investments of over 3 months in duration is compared with the average BOE base rate.

The table below illustrates the rate achieved on the two maturing investments of over three months duration in quarter 4 compared with the average base rate for the duration of the investment.

Borrower	Value £m	Period (Months)	Actual Rate (%)	Average Base Rate (%)
Landesbank Hessen-Thuringen (HELABA)	£2m	6	0.47%	0.28%
Debt Management Office (Treasury Bill)	£1m	6	0.37%	0.27%

Cash Balances: The aim of the TMSS is to invest surplus funds and minimise the level of un-invested cash balances. The actual un-invested cash balances for the period January to March are summarised in the table below:

	Number of Days	Average Balance £	Largest Balance £
Days In Credit	90	4,756	219,569
Days Overdrawn	0	0	0

The bank account had large un-invested balances on two occasions. The largest un-invested balance occurred on the 19 January (£219k) where a BACS deposit was received late in the afternoon in respect of the PFI unavailability charges. The second largest un-invested balance occurred on the 16 March (£55k) and related to a pension transfer being received by BACS.

During quarter 4 there were no occasions when the bank balance was overdrawn.

Prudential Indicators

In accordance with the Prudential Code, the TMSS includes a number of measures known as Prudential Indicators which determine if the TMSS meets the requirements of the Prudential Code in terms of *Affordability, Sustainability and Prudence*.

An analysis of the current position with regard to those prudential indicators for the financial year 2016/17 is provided at **Appendix B**. The analysis confirms that the Prudential Indicators set for 2016/17 are all being complied with.

Annual Report on Treasury Management Operations 2016/17

Treasury Strategy: In February 2016 the Commissioner approved the 2016/17 Treasury Management Strategy Statement (TMSS). The TMSS incorporated the investment and borrowing strategies for the 2016/17 financial year. The investment strategy approved for 2016/17 was largely the same as had been adopted for the previous year. The limits for each category of investment were based on the relative security of each class of financial institution and a percentage of the estimated balances, which would be available for investment during the year.

In relation to borrowing, the Commissioner has an underlying need to borrow funds to finance the capital programme, which is measured by the Capital Financing requirement (CFR). The CFR at the start of 2016/17 amounted to £18.67m (including £5.12m relating to the PFI agreement for West Cumbria TPA HQ in Workington) leaving a £13.55m exposure to external borrowing at some time into the future, which is presently being covered by the use of internal funds (reserves).

During 2016/17 the Commissioner has maintained this strategy of using cash balances, arising primarily from its reserves, to meet its cash flow commitments and was not therefore compelled to borrow. Although long term borrowing rates remained relatively low during 2016/17, a conscious decision was made to defer long term financing decisions as the short term cost of carrying debt (i.e. the differential between the borrowing rate at say 3% and the rate of under 1% available when such funding was invested) would have had an adverse effect on the revenue budget for the year and the immediate outlook period.

The Commissioner in consultation with the treasury advisors Arlingclose Ltd continues to look for the most opportune time to undertake any borrowing.

Key Statistics

Principal: During 2016/17 a total of 242 investments were placed amounting to £152.12m (2015/16 244 investments amounting to £160.21m).

Of these investments, 94 were to external counterparties and as such

will have attracted a £10 transfer fee per transaction. The transfer to the NatWest Liquidity Select account for overnight money is classed as an 'inter-account transfer' as the NatWest holds the Commissioner's main bank account. This type of transfer is free although we do pay a small fee to access the internet banking site.

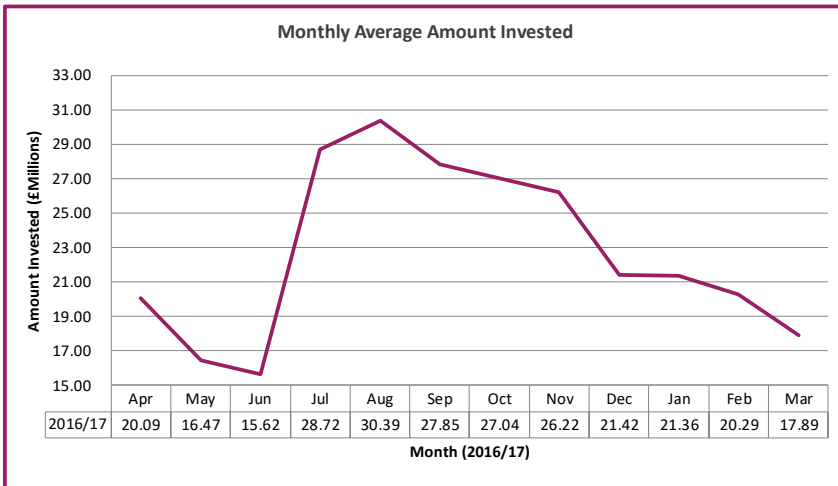
The **average** daily investment balance during 2016/17 was **£22.80m** (£24.29m in 2015/16).

The **highest** daily investment balance in 2016/17 was **£33.76m** (£34.28m in 2015/16)

The **lowest** daily investment balance in 2016/17 was **£11.32m** (£13.20m in 2015/16).

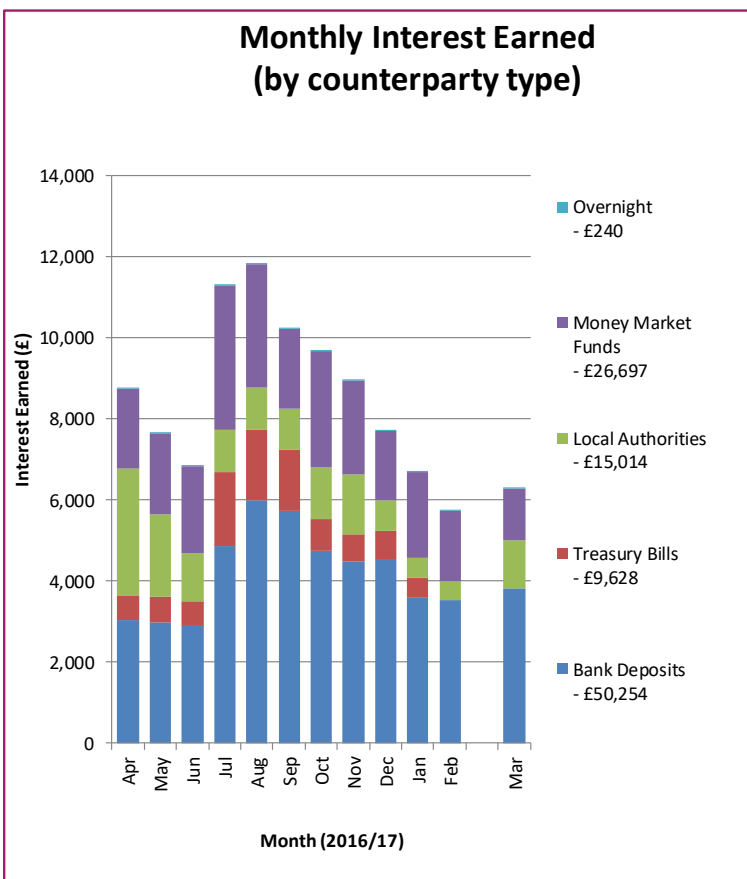
A detailed breakdown of the closing balance invested as at 31 March 2017 is provided at **Appendix A**.

The level of cash reserves available to invest has followed the same pattern as seen in previous years. The Home Office Police Pensions Grant is received in July each year and has caused an annual spike in investments since 2007/08 when new regulations were introduced.



This chart illustrates the monthly average amounts invested during 2016/17.

Interest: A total of £102k was earned in 2016/17 (£123k in 2015/16) from the Commissioner’s treasury management activities and can be broken down as follows:



Month	Interest Earned (£)
Apr	8,780
May	7,662
Jun	6,869
Jul	11,317
Aug	11,839
Sep	10,242
Oct	9,711
Nov	8,976
Dec	7,708
Jan	6,686
Feb	5,744
Mar	6,301
	101,833

The average return on investments for 2016/17 was 0.45% (0.51% in 2015/16) which is slightly above the average bank base rate for the year of 0.34%. The base rate was reduced from 0.50% to 0.25% on 4 August 2016.

The table above shows the outturn on investment interest as £102k for 2016/17, which is £2k above a base budget of £100k. The slight increase compared to the budget is as a result of interest rates not falling as quickly as had been anticipated and some investments being secured at relatively favourable rates before the reduction took effect.

Treasury Operations: As discussed above the aim of the Treasury Management Strategy is to invest surplus cash and minimise the level of un-invested cash balances, whilst limiting risks to the Commissioner’s funds. Actual un-invested balances for 2016/17 for the Commissioner’s main bank account are summarised in the table below:

	Number of Days	Average Balance	Largest Balance
		£	£
Days In Credit	356	6,768	1,603,080
Days Overdrawn	9	19,012	56,619

The largest credit balance occurred during the first quarter, the largest overdrawn balance occurred during the second quarter. The explanations are provided below and were provided in the relevant quarterly activity report to the Commissioner and Members.

The largest un-invested balance occurred on the 10 June for three days over the weekend (£1.6m). This was as a result of an error by one of the constabulary’s brokers. Investments were placed with Standard life (£1.6m) and Aberdeen asset management (£2m) on the 7 June 2016 via the broker. The broker did not advise the fund managers of our subscription. As a result the Aberdeen investment was placed one day late and Standard Life returned the funds at the close of banking on Friday 10 June. The funds were immediately reinvested on the Monday morning with Standard Life and the broker has agreed to reimburse us for the lost interest on both accounts and the additional Chaps fee totalling £174.

The largest overdrawn balance occurred on the 2 September 2016 and resulted in the main fund bank account being overdrawn by £57k over 3 days of the weekend. This was due to human error which resulted in the daily transfer to the liquidity select account not being confirmed.

Compliance with Prudential Indicators

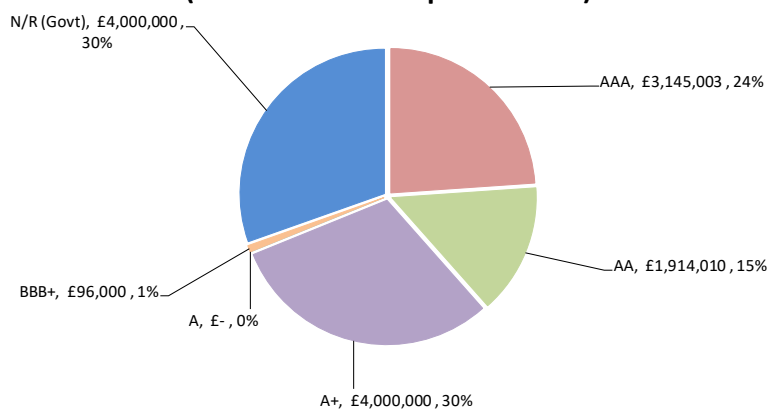
All treasury related Prudential Indicators for 2016/17, which were set in February 2016 as part of the annual Statement of Treasury Management Strategy, have been complied with. Further details can be found at **Appendix B**.

Appendix A

Investment Balance at 31 March 2017

Category/Institution	Credit Rating	Investment Date	Investment Matures	Days to Maturity	Rate (%)	Amount (£)	Counterparty Total (£)
Category 1 - Banks Unsecured (Includes Banks & Building Societies)							
Landesbank- Hessen-Thuringen (Heleba)	A+	11/01/2017	11/04/2017	11	0.24%	2,000,000	2,000,000
Lloyds Bank Plc	A+	11/08/2016	11/08/2017	133	1.00%	2,000,000	2,000,000
Svenska (Deposit Account)	AA	Various	On Demand	N/A	0.35%	1,914,010	1,914,010
NatWest (Liquidity Select Account)	BBB+	31/12/2016	01/01/2017	O/N	0.25%	96,000	96,000
						6,010,010	6,010,010
Category 2 - Banks Secured (Includes Banks & Building Societies)							
Leeds Building Society (Bond)	AAA	13/07/2016	17/12/2018	626	0.68%	2,141,288	2,141,288
						2,141,288	2,141,288
Category 3 - Government (Includes HM Treasury and Other Local Authorities)							
East Dunbartonshire Council	NR	07/03/2017	06/03/2018	340	0.50%	2,000,000	2,000,000
Highland District Council	NR	14/10/2016	18/04/2017	18	0.30%	2,000,000	2,000,000
						4,000,000	4,000,000
Category 4 - Registered Providers (Includes Providers of Social Housing)							
None						0	0
						0	0
Category 5 - Pooled Funds (Includes AAA rated Money Market Funds)							
Fidelity	AAA	Various	On demand	O/N	0.43%	3,715	3,715
Standard Life (Formally Ignis)	AAA	Various	On demand	O/N	0.51%	1,000,000	1,000,000
						1,003,715	1,003,715
Total						13,155,013	13,155,013

Analysis of Outstanding Investments by Credit Rating of Counterparty at 31 March 2017 (Minimum Criteria per TMSS A-)



Note – The credit ratings in the table & chart relate to the standing as at 31 March 2017, these ratings are constantly subject to change.

Appendix B

Prudential Indicators 2016/17

Prudential Indicator		Limits TMSS £m	Limits Revised at year end £m	Limits Revised at Sep-16 £m	Actual £m	Within Target	
1	Net Borrowing and the Capital Financing Requirement						
	This indicator is to ensure that net borrowing will only be for capital puposes. The commissioner should ensure that the net external borrowing does not exceed the total CFR requirement from the preceeding year plus any additional borrowing for the next 2 years.	Net Debt (section 9 below provides analysis)	(8.492)	(17.192)	(17.567)	(8.143)	✓
		Capital Financing Requirement as at 31 March	18.360	18.401	18.401	18.401	✓
2	Capital Expenditure and Capital financing						
	<i>The original and current forecasts of capital expenditure and the amount of capital expenditure to be funded by prudential borrowing for 2016/17</i>	Expenditure	6.883	8.553	5.027	3.034	✓
3	Ratio of Financing Costs to Net Revenue Stream						
	<i>This is an indicator of affordability and highlights the revenue implications of exisiting and proposed capital expenditure by identifying the proportion of revenue budget required to meet financing costs</i>	Financing Costs	0.313	0.313	0.323	0.311	✓
		Net Revenue Stream	95.675	95.675	95.675	96.131	✓
		Ratio	0.33%	0.33%	0.34%	0.32%	✓
4	Capital Financing Requirement						
	<i>The CFR is a measure of the extent to which the commissioner needs to borrow to support capital expenditure only. It should be noted that at present all borrowing has been met internally.</i>	CFR including PFI & other long term liabilities	18.360	18.401	18.401	18.401	✓
5	The Authroised Limit						
	<i>The authorised limit represents an upper limit of external borrowing that could be afforded in the short term but may not sustainable. It is the expected amximum borrowing need with some headroom for unexpected movements. This is a statutory limit</i>	CFR excluding PFI & other long term liabilities	13.348	13.514	13.514	13.514	✓
6	The Operational Boundry						
	<i>The operational boundry respresents and estimate of the most likely but not worse case scenario it is only a guide and may be breached temporarily due to variations in cashflow.</i>	Total Authorised Limit	24.860	24.901	24.901	24.901	✓
7	Actual External Debt						
	<i>It is unlikely that the Commissioner will actually exercise external borrowing until there is a change in the present structure of investment rates compared to the costs of borrowing</i>	Total Operational Boundry	23.360	23.401	23.401	23.401	✓
8	Impact of capital investment decisions on the Council Tax						
	<i>This indicates the incremental impact of the capital investment decisions funded from prudential borrowing proposed for the period 2016/17 based on a Band D property in line with the proposed council tax level.</i>	External Debt including PFI & other long term liabilities	5.012	5.012	5.012	5.012	✓
9	Gross and Net Debt						
	<i>The purpose of this indicator is highlight a situation where the Commissioner is planning to borrow in advance of need.</i>	External Debt excluding PFI & other long term liabilities	0.000	0.000	0.000	0.000	✓
		Capital Expenditure funded from revenue	1.534	1.534	0.508	0.544	✓
		Incremental Impact on Band D Council Tax	9.146	9.146	3.029	9.485	✓
		Outstanding Borrowing (at notional value)	0.000	0.000	0.000	0.000	✓
10/11	Interest Rate Exposure						
	<i>The purpose of this indicator is to contain the Commissioners exposure to unfavourable movements in future interset rates.. This represents the position that all of the Commissioner's auhorised external borrowing may be at a fixed rate at any one time.</i>	Other Long Term Liabilities (PFI & Finance Lease)	5.012	5.012	5.012	5.012	✓
12	Maturity Structure of Borrowing						
	<i>The indicator is desgigned to exercise control over the Commissioner having large consentrations of fixed rate debt needing to be repaid at any one time.</i>	Less Investments	13.504	22.204	22.579	13.155	✓
13	Upper Limit for total principal sums invested for over 364 Days						
	<i>The purpose of this indicator is to ensure that the commissioner has protected himself against the risk of loss arising from the need to seek early redemption of principl sums invested.</i>	Net Debt	(8.492)	(17.192)	(17.567)	(8.143)	✓
10/11	<i>The purpose of this indicator is to contain the Commissioners exposure to unfavourable movements in future interset rates.. This represents the position that all of the Commissioner's auhorised external borrowing may be at a fixed rate at any one time.</i>	Net Principal sums Outstanding at Fixed Rates	24.860	24.901	24.901	24.901	✓
		Net Principal sums Outstanding at Variable Rates	1.500	1.500	1.500	1.500	✓
12	<i>The indicator is desgigned to exercise control over the Commissioner having large consentrations of fixed rate debt needing to be repaid at any one time.</i>	Not Applicable - currently no external debt					✓
13	<i>The purpose of this indicator is to ensure that the commissioner has protected himself against the risk of loss arising from the need to seek early redemption of principl sums invested.</i>	Non Specified Investments with a maturity greater than 364 days					✓
			5.000	5.000	5.000	4.200	✓