Peter McCall

Treasury Management Activities 2017/18 Quarter 4 (January to March 2018) and Annual Report 2017/18

Public Accountability Conference 10 May 2018 and JASC Meeting 24 May 2018

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 2018, 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

The UK economy has showed signs of slowing with latest estimates of GDP growing by 1.8% in 2017 (the same level as in 2016). This was far better than the majority of forecasts following the EU referendum in June 2016. The Bank of England (BOE) Base Rate was increased from 0.25% to **0.50%** on 1 November 2017, the first rate rise in 10 years.

The treasury advisor's Arlingclose central case is for the Bank Base Interest Rate to gradually climb towards 1.25% by summer 2019 and then remain at this level for a period of time.

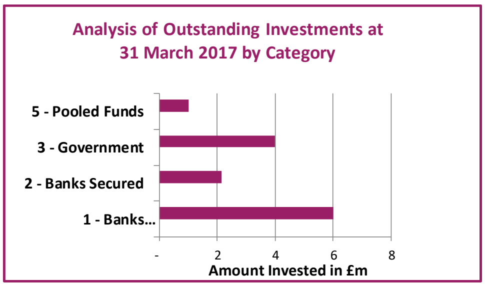
Consumer Price Index (CPI) inflation rose to 3.1% in November before falling back to 2.7% in February. The February inflation report indicated that the MPC were keen to return inflation to the target 2% over a more conventional 18-24 month period with 'gradual' and 'limited' policy tightening. The minutes of the March MPC meeting suggested that an increase in interest rates in May 2018 was highly likely, however recent weakness in growth figures may delay this decision.

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 2018 the total value of investments was **£15.807m** 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 £15.807m is provided at **Appendix A**.

Investment Activity: During quarter 4 a total of 6 investments with a combined value of £12.9m 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 £4.1m. Of these two, neither has an outstanding duration of over 364 days. These investments are:

- Leeds Building Society £2.1m 887 days (13/07/16 to 17/12/18)
- Lancashire County Council £2m (18/04/17 to 17/04/18)

Investment Income: The budget for investment interest receivable in 2017/18 was £75k. The actual income achieved against this target was £90k which provides an excess of £15k (20%). Previous reports forecast that investment income would be on budget. The increase against budget is largely due to the increase in interest rates in November.

The average return on investment during quarter 4 was 0.44%. 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 for the period of the investment.

The table below illustrates the rate achieved on the five 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 (%)
Moray Council	£2m	4.2	0.28%	0.43%
Treasury Bill	£4m	6.0	0.23%	0.35%
Treasury Bill	£2m	6.0	0.20%	0.36%
Nationwide	£2m	3.0	0.37%	0.50%
East Dunbartonshire	£2m	12.0	0.50%	0.34%

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	82	2,727	33,228
Days Overdrawn	8	(935,805)	(2,098,726)

The bank account had only one larger un-invested balance during quarter 4. This was for an amount of £33k and occurred on 25 January and was in relation to a number of un-anticipated cash bankings being made by central services and area staff.

During quarter 4 there were three occasions where the bank balance was substantially overdrawn. The first instance occurred over the weekend of 16-18 February for £1.4m, this was as a result of an error by treasury staff whereby an online transaction to withdraw money market funds (MMF) was only partially completed. The second instance occurred on 28 February for £2.1m, this was as a result of an error by the broker whereby requested funds were not repaid, the broker has agreed to pay all charges in respect of this error (£86). The final instance occurred over the weekend of 16-18 March for £397k and was again as a result of an error by treasury staff where a withdrawal from MMF was not transacted. The estimated interest incurred as a result of the unauthorised overdraft usage in respect of the first and third item above is £220.

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 2017/18 is provided at **Appendix B**.

The analysis confirms that the Prudential Indicators set for 2017/18 are all being complied with.

Annual Report on Treasury Management Operations 2017/18

Treasury Strategy: In February 2017 the Commissioner approved the 2017/18 Treasury Management Strategy Statement (TMSS). The TMSS incorporated the investment and borrowing strategies for the 2017/18 financial year. The investment strategy approved for 2017/18 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 2017/18 amounted to £18.40m (including £5.01m relating to the PFI agreement for West Cumbria TPA HQ in Workington) leaving a £13.39m exposure to external borrowing at some time into the future, which is presently being covered by the use of internal funds (reserves).

During 2017/18 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 2017/18, 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 longer term borrowing.

Key Statistics

Principal: During 2017/18 a total of 220 investments were placed amounting to £149.32m (2016/17 242 investments amounting to £152.12m).

Of these investments, 64 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.

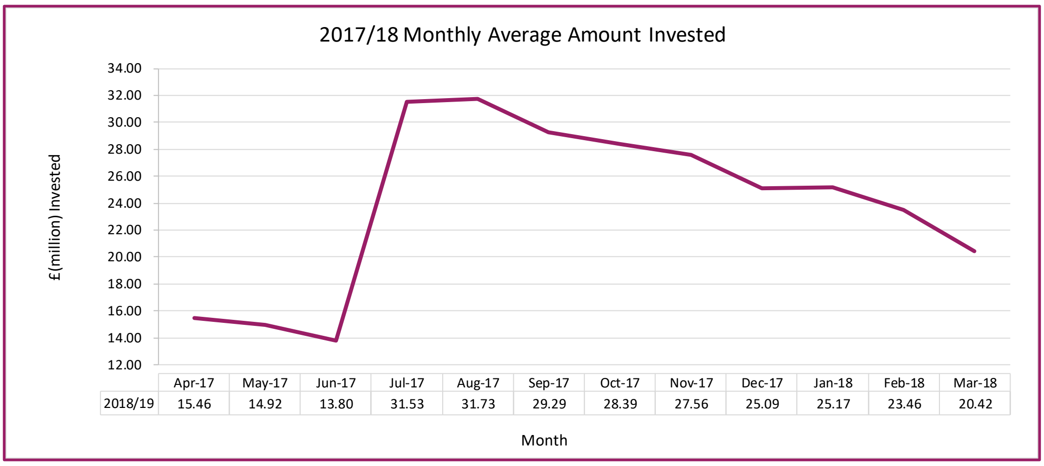
The **average** daily investment balance during 2017/18 was **£23.93m** (£22.80m in 2016/17).

The **highest** daily investment balance in 2017/18 was **£36.24m** (£33.76m in 2016/17)

The **lowest** daily investment balance in 2017/18 was **£9.68m** (£11.32m in 2016/17).

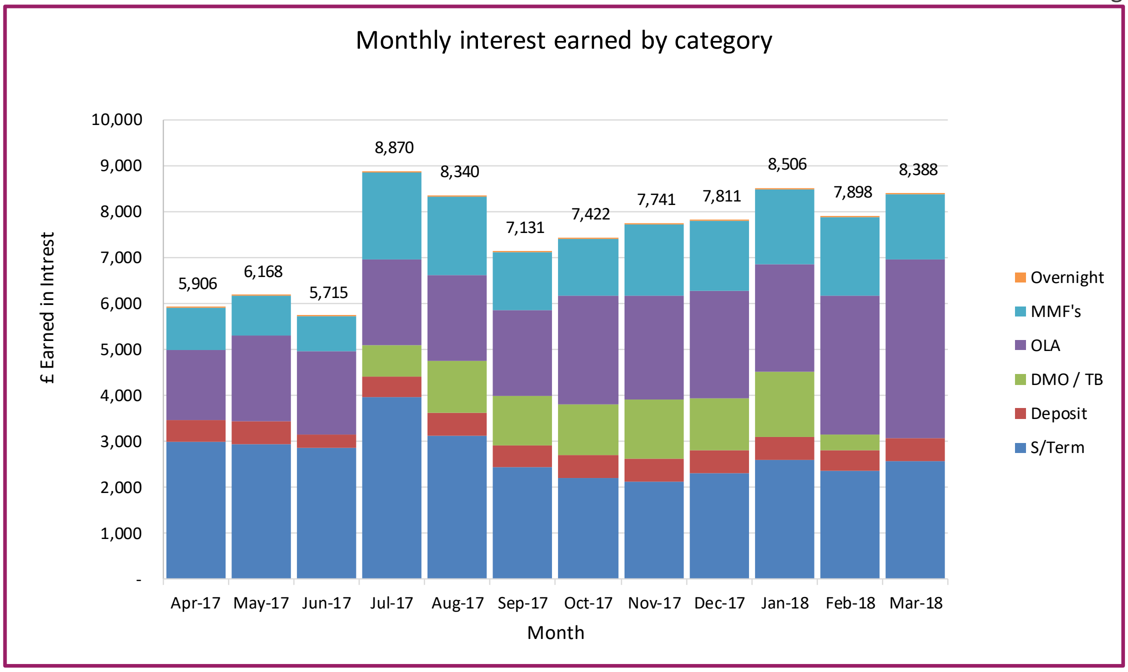
A detailed breakdown of the closing balance invested as at 31 March 2018 is provided at Appendix A.

The level of cash reserves available to invest has followed the same pattern as seen in previous years. Following the introduction of the Home Office Police Pensions Grant in 2007/08, there has been an annual spike in investments in July, when the majority of the grant is received, followed by a gradual decline in balances as pension payments are made throughout the remainder of the year.



This chart illustrates the monthly average amounts invested during 2017/18.

Interest: A total of £90k was earned in 2017/18 (£102k in 2016/17) from the Commissioner's treasury management activities and can be broken down as follows:



The average return on investments for 2017/18 was 0.38% (0.45% in 2016/17) which is slightly above the average bank base rate for the year of 0.35%. The base rate was increased from 0.25% to 0.50% on 1 November 2017.

The table above shows the outturn on investment interest as £90k for 2017/18, which is £15k above a base budget of £75k. The increase compared to the budget is largely as a result of interest rates increasing part the way through the year, which was not forecast when the strategy was produced.

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 2017/18 for the Commissioner's main bank account are summarised in the table below:

	Number of Days	Average Balance £	Largest Balance £
Days In Credit	351	6,623	417,825
Days Overdrawn	14	(652,519)	(2,098,726)

The largest credit balance occurred during quarter three, the largest overdrawn balance occurred during the fourth 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 27 November (£418k) when a capital receipt in respect of the sale of the former police station at Barrow was received without notification.

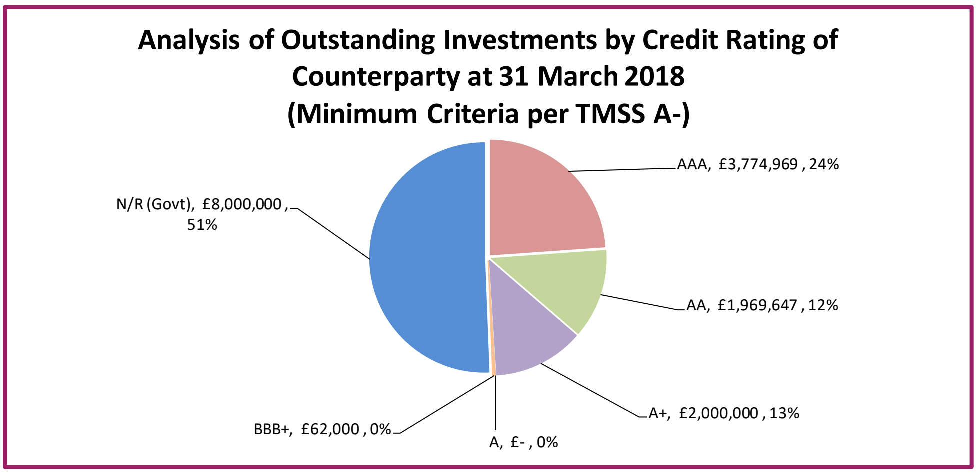
As outlined on page 2 above, the largest overdrawn balance occurred on 28 February for £2.1m, this was as a result of an error by the broker whereby requested funds were not repaid, the broker has agreed to pay all charges in respect of this error.

Compliance with Prudential Indicators

All treasury related Prudential Indicators for 2017/18, which were set in February 2017 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 2018

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 (Helaba)	A+	07/12/2017	31/05/2018	61	0.45%	2,000,000	2,000,000
Svenska (Deposit Account)	AA	Various	On Demand	N/A	0.30%	1,969,647	1,969,647
NatWest (Liquidity Select Account)	BBB+	31/03/2018	01/04/2018	O/N	0.05%	62,000	62,000
						4,031,647	**4,031,647**
Category 2 - Banks Secured (Includes Banks & Building Societies)							
Leeds Building Society (Bond)	AAA	13/07/2016	17/12/2018	261	0.68%	2,070,884	2,070,884
						2,070,884	**2,070,884**
Category 3 - Government (Includes HM Treasury and Other Local Authorities)							
East Dunbartonshire Council	NR	06/05/2018	06/09/2018	159	0.80%	2,000,000	2,000,000
Salford City Council	NR	05/02/2018	08/05/2018	38	0.45%	2,000,000	2,000,000
The Moray Council	NR	31/01/2018	30/04/2018	30	0.50%	2,000,000	2,000,000
Lancashire County Council	NR	18/04/2017	17/04/2018	17	0.60%	2,000,000	2,000,000
						8,000,000	**8,000,000**
Category 5 -Pooled Funds (Includes AAA rated Money Market Funds)							
Fidelity	AAA	Various	On demand	O/N	0.38%	4,085	4,085
Goldman Sachs	AAA	Various	On demand	O/N	0.35%	100,000	100,000
Aberdeen Asset Management	AAA	Various	On demand	O/N	0.36%	1,600,000	1,600,000
						1,704,085	**1,704,085**
Total						**15,806,616**	**15,806,616**



Note – The credit ratings in the table & chart relate to the standing as at 31 March 2018, these ratings are constantly subject to change.

Appendix B
Prudential Indicators 2017/18

	Prudential Indicator - With Targets To Review	Indicator	Approved Indicators TMSS	Current Value	Within Target
1	**The Authorised Limit** *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 maximum borrowing need with some headroom for unexpected movements. This is a statutory limit*	Total Authorised Limit (£m)	24.480	4.745	✓
2	**The Operational Boundary** *The operational boundary represents 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 cash flow.*	Total Operational Boundary (£m)	22.978	4.745	✓
3/4	**Interest Rate Exposure** *The purpose of this indicator is to contain the Commissioners exposure to unfavourable movements in future interest rates.. This represents the position that all of the Commissioner's authorised external borrowing may be at a fixed rate at any one time.*	Net Principal sums Outstanding at Fixed Rates (£m)	24.480	4.745	✓
		Net Principal sums Outstanding at Variable Rates (£m)	1.500	0.000	✓
5	**Upper Limit for total principal sums invested for over 364 Days** *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 principal sums invested.*	Non Specified Investments with a maturity greater than 364 days (£m)	5.000	4.100	✓
	Prudential Indicator - To Note				
6	**Net Borrowing and the Capital Financing Requirement** This indicator is to ensure that net borrowing will only be for capital purposes. The commissioner should ensure that the net external borrowing does not exceed the total CFR requirement from the preceding year plus any additional borrowing for the next 2 years.	Net Debt (section 12 below provides analysis) (£m)	(15)	(19.188)	
		Capital Financing Requirement as at 31 March (£m)	17.978	17.980	
		Net external Borrowing (£m)	0.000	0.000	
7	**Capital Expenditure and Capital financing** *The original and current forecasts of capital expenditure and the amount of capital expenditure to be funded by prudential borrowing for 2017/18*	Expenditure (£m)	6.521	5.254	
		Financing and Funding (£m)	0.000	0.000	
8	**Ratio of Financing Costs to Net Revenue Stream** *This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of revenue budget required to meet financing costs*	Financing Costs (£m)	0.348	0.333	
		Net Revenue Stream (£m)	96.178	96.178	
		Ratio	0.36%	0.35%	
9	**Capital Financing Requirement** *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.*	CFR including PFI & other long term liabilities (£m)	17.978	17.980	
		CFR excluding PFI & other long term liabilities (£m)	13.091	13.093	
10	**Actual External Debt** *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*	External Debt including PFI & other long term liabilities (£m)	4.887	4.745	
		External Debt excluding PFI & other long term liabilities (£m)	0.000	0.000	
11	**Impact of capital investment decisions on the Council Tax** *This indicates the incremental impact of the capital investment decisions funded from prudential borrowing proposed for the period 2017/18 based on a Band D property in line with the proposed council tax level.*	Capital Expenditure funded from revenue (£m)	1.584	2.128	
		Incremental Impact on Band D Council Tax (£)	9.485	12.745	
12	**Gross and Net Debt** *The purpose of this indicator is highlight a situation where the Commissioner is planning to borrow in advance of need.*	Outstanding Borrowing (at notional value) (£m)	0.000	0.000	
		Other Long Term Liabilities (PFI & Finance Lease) (£m)	4.887	4.745	
		Less Investments (£m)	20.167	23.933	
		Net Debt (£m)	(15.280)	(19.188)	
13	**Maturity Structure of Borrowing** *The indicator is designed to exercise control over the Commissioner having large concentrations of fixed rate debt needing to be repaid at any one time.*	Not Applicable - currently no external debt			

This page has been left intentionally blank.