ITEM NO. 9.1

Report of:	**Head of Finance**
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Portfolio Leader:	**Leader of the Council**
Key Decision:	**No**
Report Track:	**Audit & Governance Cttee. 27/06/17 and Council 05/07/17**

COUNCIL

5 JULY 2017

ANNUAL TREASURY MANAGEMENT REPORT 2016/17

1 Purpose of Report

1.1 To update Members on treasury management activity and performance during the 2016/17 financial year.

2 Recommendations

2.1 To note the annual treasury management report for 2016/17

2.2 To approve the actual 2016/17 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 2016/17 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 2016/17. 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 2016/17 the minimum reporting requirements were that the full Council should receive the following reports:-

- an annual treasury strategy in advance of the year (Council – 16 February 2016);
- a mid year treasury update report ;
- an annual review following the end of the year describing the activity compared to the strategy (this report).

5.3 No mid year treasury report was submitted in 2016/17 however a review of Borrowing Requirements/Minimum Revenue Provision was undertaken as part of the Financial recovery plan and an amendment to the MRP policy was made as part of the 2017/18 Treasury Management strategy.

5.4 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.

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

The Economy and Interest Rates

5.6 The two major landmark events that had a significant influence on financial markets in the 2016-17 financial year were the UK EU referendum on 23 June and the election of President Trump in the USA on 9 November. The first event had an immediate impact in terms of market expectations of when the first increase in Bank Rate would happen, pushing it back from quarter 3 2018 to quarter 4 2019. At its 4 August meeting, the Monetary Policy Committee (MPC) cut Bank Rate from 0.5% to 0.25% and the Bank of England's Inflation Report produced forecasts warning of a major shock to economic activity in the UK, which would cause economic growth to fall almost to zero in the second half of 2016. The MPC also warned that it would be considering cutting Bank Rate again towards the end of 2016 in order to support growth. In addition, it restarted quantitative easing with purchases of £60bn of gilts and £10bn of corporate bonds, and also introduced the Term Funding Scheme whereby potentially £100bn of cheap financing was made available to banks.

5.7 In the second half of 2016, the UK economy confounded the Bank's pessimistic forecasts of August. After a disappointing quarter 1 of only +0.2% GDP growth, the three subsequent quarters of 2016 came in at +0.6%, +0.5% and +0.7% to produce an annual growth for 2016 overall, compared to 2015, of no less than 1.8%, which was very nearly the fastest rate of growth of any of the G7 countries. Needless to say, this meant that the MPC did not cut Bank Rate again after August but, since then, inflation has risen rapidly due to the effects of the sharp devaluation of sterling after the referendum

Overall Treasury Position as at 31 March 2017

5.8 At the beginning and the end of 2016/17 the Council's treasury position was as follows:

TABLE 1	31 March 2016 Principal	Rate/ Return	Average Life Years	31 March 2017 Principal	Rate/ Return	Average Life Years
Total debt (PWLB)	£85.0m	4.15%	38.1	£84.2m	4.18%	38.4
CFR	£96.4m	-	-	£95.8m	-	-
Over / (under) borrowing	(£11.4m)	-	-	(£11.6m)	-	-
Total investments	£12.4m	0.65%	0.34	£18.6m	0.57	0.36
Net debt	£72.6m	-	-	£65.6m	-	-

Strategy for 2016/17

5.9 The expectation for interest rates within the treasury management strategy for 2016/17 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.

5.10 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.

5.11 During 2016/17 there was major volatility in PWLB rates with rates falling during quarters 1 and 2 to reach historically very low levels in July and August, before rising significantly during quarter 3, and then partially easing back towards the end of the year.

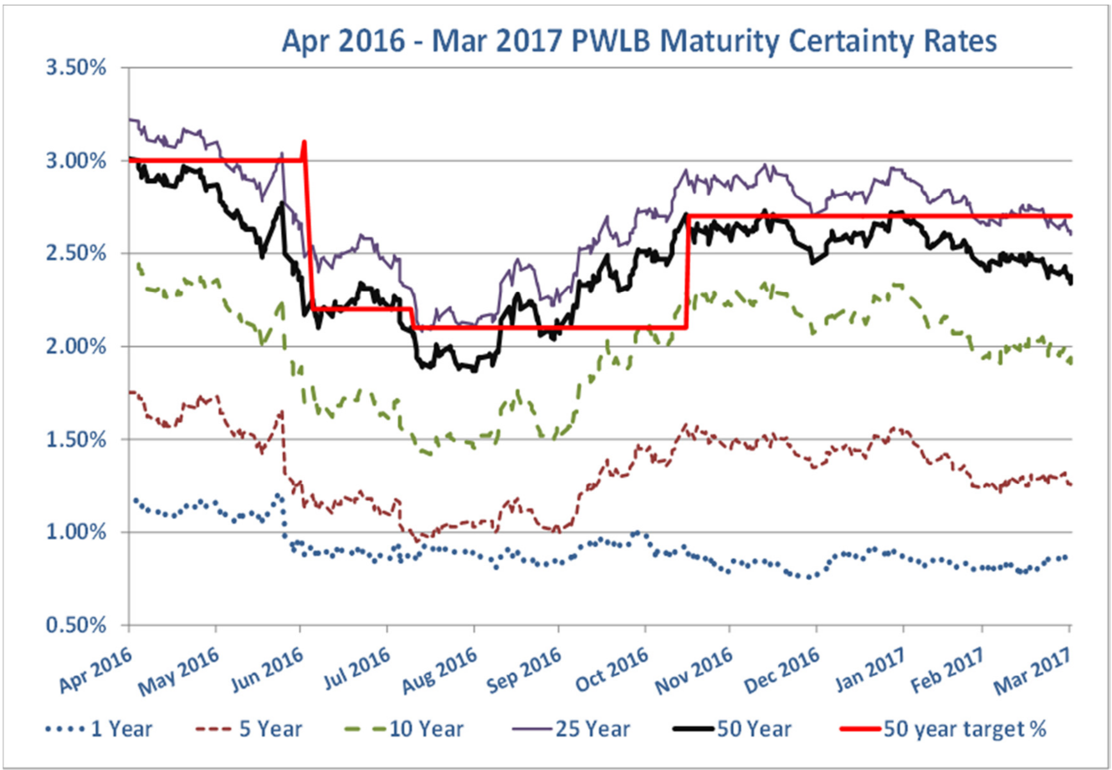
Borrowing Requirement

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

	31 March 2016 Actual	31 March 2017 Budget	31 March 2017 Actual
Capital Financing Requirement	£96.419m	£96.784m	£95.769m

Borrowing Rates in 2016/17

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

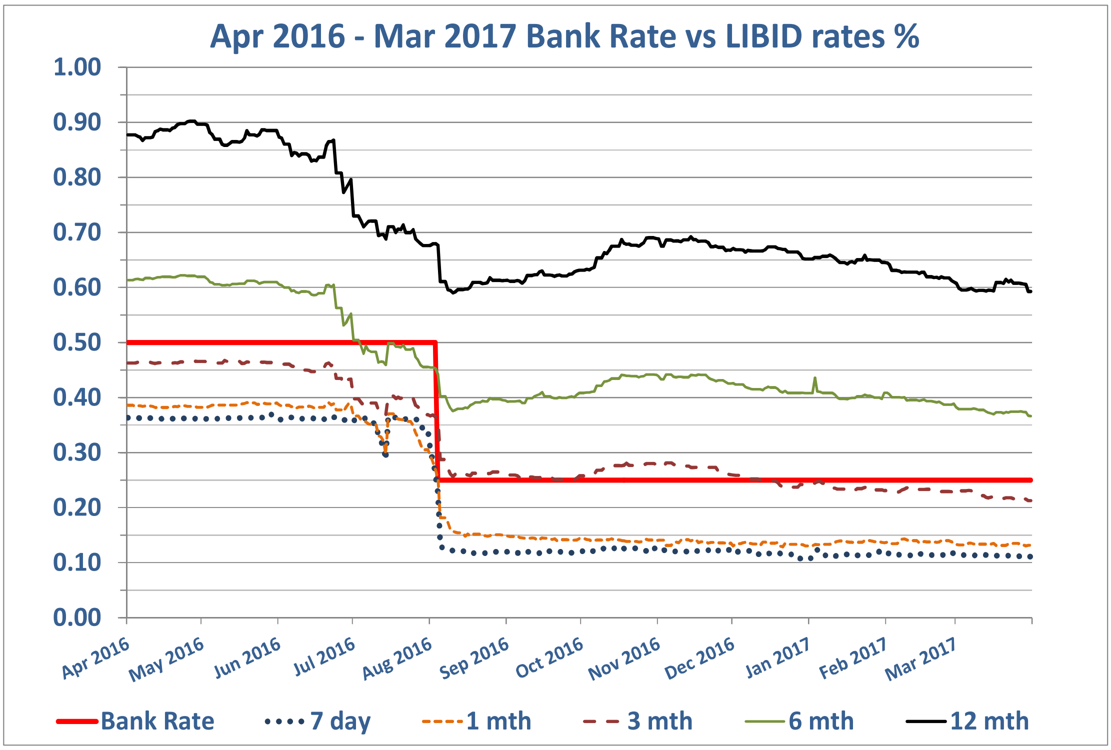


Borrowing Outturn for 2016/17

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

Investment Rates in 2016/17

5.15 After the EU referendum, Bank Rate was cut from 0.5% to 0.25% on 4 August and remained at that level for the rest of the year. Market expectations as to the timing of the start of monetary tightening started the year at quarter 3 2018, but then moved back to around the end of 2019 in early August before finishing the year back at quarter 3 2018. Deposit rates continued into the start of 2016/17 at previous depressed levels but then fell during the first two quarters and fell even further after the 4 August MPC meeting resulted in a large tranche of cheap financing being made available to the banking sector by the Bank of England. Rates made a weak recovery towards the end of 2016 but then fell to fresh lows in March 2017.



Investment Outturn for 2016/17

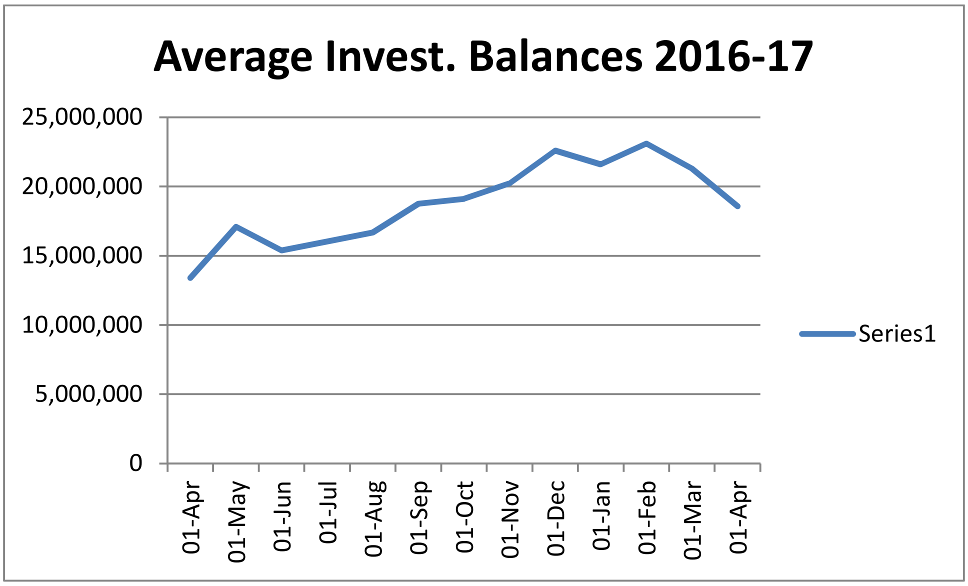
5.16 **Investment Policy** - the Council's investment policy is governed by CLG guidance, which was been implemented in the annual investment strategy approved by the Council on 16 February 2016. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

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

5.21 **Investments as at 31 March 2017** -The Council's investments as at 31 March 2017 are set out in the table below:

Counterparty	Start Date	Maturity	Value (£)	Rate %
Barclays Bank plc	Call		500,000	0.05
Standard Life (MMF)	Call		4,600,000	0.2862
Federated Prime Rate	Call		2,700,000	0.2210
Santander	95 day notice account		4,000,000	0.65
Toronto Dominion	12/05/16	11/05/17	2,000,000	0.87
Helaba	16/11/16	16/11/17	2,500,000	0.67
Bank of Scotland plc	14/03/17	13/09/17	2,276,000	0.60
TOTAL			**18,576,000**	**0.50**

5.22 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 **£28.9 million** and the average balance for the year was **£20.4 million**.



5.23 The funds earned an average rate of return for the year of **0.57%**. The comparable performance indicator is the average 3 month London Interbank rate (LIBID), which was **0.32%**. 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.

5.24 Overall investment earnings for the year totalled **£153,000**.

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: 2016-17 Prudential and Treasury Indicators

Previous Consideration

None

Background Papers

Available in Financial Services.

Appendix 1

1. PRUDENTIAL INDICATORS	**2015/16**	**2016/17**	**2016/17**
	actual	**estimate**	**actual**
	£'000	**£'000**	**£'000**
Capital Expenditure	17,335	16,340	12,207
Ratio of financing costs to net revenue stream (GF)	3.2%	4.0%	3.9%
Gross debt	85,005	86,280	84,205
Capital Financing Requirement as at 31 March	96,419	96,784	95,769
2. TREASURY MANAGEMENT INDICATORS			
Authorised Limit for external debt -	108,082	108,284	108,284
Operational Boundary for external debt	96,582	96,784	96,784
Actual external debt	85,005	86,280	84,205
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 2016/17	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%