Wiltshire Council

Cabinet

13 June 2017

Subject: **Annual Report on Treasury Management 2016/2017**

Cabinet member: **Councillor Philip Whitehead – Finance and IT**

Key Decision: **No**

<u>Executive Summary</u>

In accordance with the Chartered Institute of Public Finance and Accountancy (CIPFA) (the accountancy body for the public services) Prudential Code for Capital Finance in Local Authorities 2003 (The Prudential Code), the Council adopted a Treasury Management Strategy (TMS) for 2016/2017, including a set of Prudential and Treasury Indicators (PrIs/TrIs) and an Annual Investment Strategy (AIS) at its meeting on 23 February 2016. This report shows how the Council has performed against the strategy.

The Treasury Strategy was adhered to in 2016/2017; the average long term borrowing rate was 3.771%; and the return on short term investments was 0.455%.

<u>Proposals</u>

The Cabinet is asked to consider and note:

a) Prudential Indicators, Treasury Indicators and other treasury management strategies set for 2016/2017 against actual positions resulting from actions within the year as detailed in Appendix A; and

c) investments during the year in the context of the Annual Investment Strategy as detailed in Appendix B.

<u>Reasons for Proposals</u>

To give members of the Cabinet an opportunity to consider the performance of the Council against the parameters set out in the approved Treasury Management Strategy for 2016/2017.

This report is required by the Prudential Code for Capital Finance in Local Authorities and the CIPFA Code of Practice for Treasury Management in the Public Services.

Michael Hudson – Associate Director, Finance

Wiltshire Council

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1. Background & Purpose of Report

1.1 In accordance with the Chartered Institute of Public Finance and Accountancy (CIPFA) (the accountancy body for the public services) Prudential Code for Capital Finance in Local Authorities 2003 (The Prudential Code), the Council adopted a Treasury Management Strategy (TMS) for 2016/2017, including a set of Prudential and Treasury Indicators (PrIs/TrIs) and an Annual Investment Strategy (AIS) at its meeting on 23 February 2016.

1.2 A quarterly report for the period from 1 April to 31 December 2016 was submitted to Cabinet on 14 March 2017. This report covers the whole financial year ended 31 March 2017.

2. Main Considerations for the Cabinet

2.1 This report reviews:

a) PrIs, TrIs and other treasury management strategies set for 2016/2017 against actual positions resulting from actions within the year (see Appendix A); and

b) investments during the year in the context of the Annual Investment Strategy (see Appendix B).

2.2 There were no opportunities to restructure Public Works Loan Board (PWLB) loans in 2016/2017, mainly because of the continuing high level of premiums payable for early repayment.

Review of Prudential and Treasury Indicators and Treasury Management Strategy for 2016/2017

2.3 The detail of the review is given in Appendix A. The Cabinet is asked to note that:

a) all action has been within the approved PrIs and TrIs;

b) the average interest rate for long term debt has marginally increased (from 3.769%) to 3.771%, the increase being due to the maturity of two PWLB loans, both of which were at a slightly lower rate. The amount of loans outstanding has reduced by £12 million between 1 April 2016 and 31 March 2017;

c) short term cash deficits and surpluses were managed through temporary loans and deposits with a return on short term investments of 0.46% (a decrease from 0.56% in 2015/2016, reflecting decreases in the market during the year). This compares with the average market rate, based on the Average 3 Month LIBID Rate for 2016/2017 (London Interbank Bid Rate, i.e. the rate at which banks are prepared to borrow from other banks) of 0.32% (0.46% for 2015/2016); and

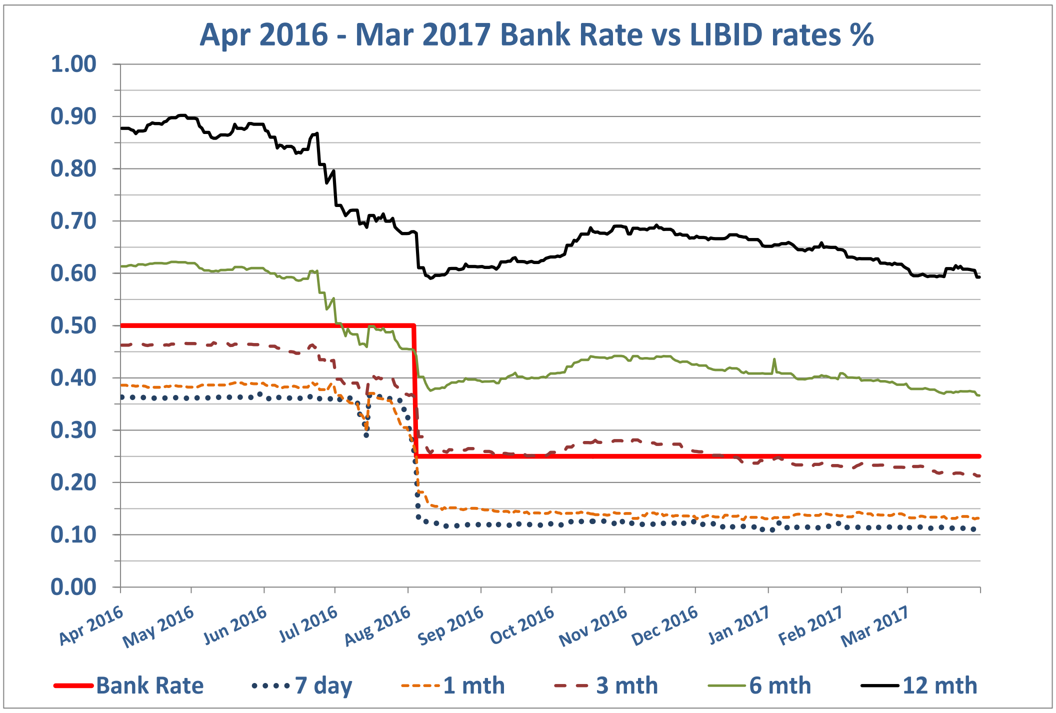
Review of Investment Strategy

2.4 This review is detailed in Appendix B. The Cabinet is asked to note that:

a) The financial year 2016/2017 continued the challenging investment environment of previous years, namely low investment returns.

b) In August 2016 the Bank of England cut the Bank Rate for the first time since 2009 to 0.25%. Capita are currently projecting that the start of monetary tightening (when the Bank of England is expected to start raising interest rates) will occur in June 2019. However, under current market conditions this is difficult to predict.

c) Deposit rates continued into the start of 2016/2017 at previous depressed levels, but then fell during the first two quarters, and then fell even further following the bank rate cut. The chart below details (investment) rates, as measured by the London Interbank Bid (LIBID) rate (i.e. the bid rate banks are willing to pay other banks for deposits in the London interbank market).



3. Safeguarding Implications

3.1 None have been identified as arising directly from this report.

4. Public Health Implications

4.1 None have been identified as arising directly from this report.

5. Corporate Procurement Implications

5.1 None have been identified as arising directly from this report.

6. Equalities Impact of the Proposal

6.1 None have been identified as arising directly from this report.

7. Environmental and Climate Change Considerations

7.1 None have been identified as arising directly from this report.

8. Risks Assessment and Financial Implications

8.1 The primary treasury management risks to which the Council is exposed are adverse movements in interest rates and the credit risk of counterparties.

8.2 Investment counterparty[1] risk is controlled by assessing and monitoring the credit risk of borrowers as authorised by the Annual Investment Strategy. Appendix B of this report details action taken in 2016/2017.

8.3 At 31 March 2017, the Council's average interest rate in respect of long term debt was 3.771%.

8.4 It is also considered important to ensure that there is an even spread of loans to avoid the prospect of a number of high value loans maturing in any one year, which may need to be re-financed at a time when interest rates are high. A summary of the present loan maturity profile is shown in Appendix C (i).

8.5 Returns on short term investments have not moved significantly, mainly as a result of the volatility of the market following the 'credit crunch' starting in October 2008 and are likely to continue at near current levels for some time. The costs of borrowing for the Council have remained at similar levels because the loan profile is almost entirely at fixed maturity rates. The investment rate of return for the year was 0.46%, against the average borrowing rate of 3.771%.

9. Legal Implications

9.1 None have been identified as arising directly from this report.

10. Options Considered

10.1 The availability of any longer term investment opportunities, such as those offered by "special tranche rates", is continually monitored.

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[1] A Counterparty is a term most commonly used in the financial services industry to describe a legal entity, unincorporated entity or collection of entities (e.g. lender/borrower) to which an exposure to financial risk might exist.

10.2 Also any options available to provide savings from rescheduling long term borrowing are continually assessed in liaison with our treasury advisers.

11. Conclusion

11.1 Cabinet is asked to note the report.

Michael Hudson
Associate Director, Finance

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Background Papers

The following unpublished documents have been relied on in the preparation of this Report: NONE

Appendices

Appendix A Review of Prudential and Treasury Indicators for 2016/2017
Appendix B Review of Investment Strategy for 2016/2017
Appendix C Summary of Long Term Loans, Temporary Loans and Deposits for 2016/2017

APPENDIX A

REVIEW OF PRUDENTIAL AND TREASURY INDICATORS FOR 2016/2017

1. Where appropriate the figures shown in this report are consistent with the PrI and TrI estimates in the Strategy for the next three years, as reviewed and reported as part of the 2016/2017 budget process.

Prudential Indicators

PrI 1 - Capital Expenditure

2. The table below shows the original and revised estimate of capital expenditure against the actual for the year 2016/2017:

	2016/2017 Original Estimate £million	2016/2017 Revised Estimate £million	2016/2017 Actual Outturn £million
General Fund	111.8	92.1	61.1
Housing Revenue Account	42.5	23.1	18.9

3. The Capital Programme has been actively managed throughout the year and the revised capital budget (capital outturn position for 2016/2017) is £80.03 million. Further breakdown of these figures is presented in the capital outturn report, elsewhere on the Cabinet agenda.

PrI 2 – Ratio of Financing Costs to Net Revenue Stream

4. PrI 2 expresses the net costs of financing as a percentage of the funding receivable from the Government and council tax payers (General Fund) and rents receivable (HRA). The net cost of financing includes interest and principal repayments for long and short term borrowing, as well as other credit-like arrangements, netted off by interest receivable from cash investments.

	2016/2017 Original Estimate	2016/2017 Revised Estimate	2016/2017 Actual
General Fund	8.1%	7.3%	7.2%
Housing Revenue Account	15.2%	15.0%	15.0%

5. In terms of the General Fund, slight differences between budgeted and actual costs led to a minor decrease in actual ratio when compared with the original estimate.

PrI 3 – Estimate of Incremental Impact of Capital Investment Decisions on the Council Tax

6. This indicator is only relevant during budget setting, as it reflects the impact on the Band D Council Tax, or average weekly housing rents in respect of the HRA, caused by any agreed changes in the capital budget.

PrI 4 – Gross Borrowing and the Capital Financing Requirement

7. PrI 4 measures the so called “Golden Rule” which ensures that borrowing is only for capital purposes.

	2016/2017 Original Estimate £million	**2016/2017 Revised Estimate £million**	**2016/2017 Actual £million**
CFR – General Fund	439.1	413.7	383.6
CFR – HRA	122.6	123.3	123.3
Gross Borrowing – Gen Fund	314.1	262.9	219.1
Gross Borrowing – HRA	118.8	118.8	118.8
CFR not funded by gross borrowing – Gen Fund	**125.0**	**150.8**	**164.5**
CFR not funded by gross borrowing – HRA	**3.8**	**4.5**	**4.5**

8. The Capital Financing Requirement (CFR) increases whenever capital expenditure is incurred. If resourced immediately (from capital receipts, direct revenue contributions or capital grant/contributions) the CFR will reduce at the same time that the capital expenditure is incurred, with no net increase in CFR.

9. Where capital expenditure is not resourced immediately, there is a net increase in CFR, represented by an underlying need to borrow for capital purposes, whether or not external borrowing actually occurs. The CFR may then reduce over time by future applications of capital receipts, capital grants/contributions or further charges to revenue.

10. This PrI is necessary, because under an integrated treasury management strategy (in accordance with best practice under the CIPFA Code of Practice on Treasury Management in the Public Services), borrowing is not associated with particular items or types of expenditure, whether revenue or capital

11. The difference between actual external (gross) borrowing (£219.1 million) and the CFR (CFR not funded by gross borrowing above) is capital expenditure met by internal borrowing, i.e. funded from the Council’s own funds, such as reserves and balances and working capital (an accounting term for the difference, at a point in time, between what the Council owes and what is owed to it).

12. Internal borrowing is cheaper than external borrowing (see paragraph 8.5 of the main report), however, the ability to borrow internally will depend upon the sufficiency of reserves, balances and working capital. The sufficiency needs to be monitored and projections carried out to indicate where any adverse movements are expected, that could jeopardise the Council’s cash flow position, making it necessary to replace internal with external borrowing.

PrI 5 – Compliance with CIPFA Code of Practice for Treasury Management in the Public Services (“The Code”)

In the past year the Council was fully compliant with the CIPFA Code of Practice for Treasury Management in the Public Services.

13. This Code of Practice has been complied with during 2016/2017.

Treasury Management Indicators within the Prudential Code

TrI 1 – Authorised Limit for External Debt

Authorised Limit	**2016/2017 £million**	**2017/2018 £million**	**2018/2019 £million**
Borrowing – General Fund	471.7	483.0	466.6
Borrowing – HRA	123.2	123.2	123.2
Total Borrowing	**594.9**	**606.2**	**589.8**
Other Long Term Liabilities	0.2	0.2	0.2
TOTAL	**595.1**	**606.4**	**590.0**

14. This Authorised Limit was not exceeded at any time during the year, as maximum borrowing was below the (lower) Operational Boundary.

TrI 2 – Operational Boundary for External Debt

Operational Boundary	**2016/2017 £million**	**2017/2018 £million**	**2018/2019 £million**
Borrowing – General Fund	460.2	471.2	455.2
Borrowing – HRA	123.2	123.2	123.2
Total Borrowing	**583.4**	**594.4**	**578.4**
Other Long Term Liabilities	0.2	0.2	0.2
TOTAL	**583.6**	**594.6**	**578.6**

15. This TrI is for gross borrowing and was set at a limit that would allow the Council to take its entire financing requirement as loans if this was the most cost effective alternative. The limit on HRA borrowing is capped in 2016/2017 at £123.2 million. The limits, which have not been exceeded during the period covered by this report, are set to anticipate expected expenditure. The maximum gross borrowing during the year being £349.9 million (£231.1 million on General Fund and £118.8 on HRA) at the beginning of the financial year up to 31 May 2016.

TrI 3 – External Debt

	2015/2016 Actual £million	**2016/2017 Expected £million**	**2016/2017 Actual £million**
Borrowing – General Fund	231.1	262.9	219.1
Borrowing – HRA	118.8	118.8	118.8
Total Borrowing	349.9	381.7	337.9
Other Long Term Liabilities	£0.2	0.2	£0.2
TOTAL	350.1	381.9	338.1

16. This TrI shows the gross External Debt outstanding at year end. The actual borrowing figure is outstanding long term borrowing as shown in Appendix C (i). Actual borrowing was less than expected at the end of 2016/2017, partially due to the reduced borrowing position as a result of not refinancing the maturing PWLB loans, together with the actual underlying borrowing requirement for capital projects being lower than anticipated.

17. As can be seen in the above table, actual General Fund Borrowing has decreased by £12 million this financial year. Two PWLB loans matured during 2016/2017, a £2 million loan in June 2016 and a £10 million loan in March 2017, neither were refinanced.

Treasury Management Indicators within the Treasury Management Code

TrI 4a and 4b – Upper Limit on Fixed Interest Rate Exposures and Interest Rate Exposures, respectively

The Council's upper limit for fixed interest rate exposure for the period 2016/2017 to 2018/2019 is 100% of net outstanding principal sums.

The Council's upper limit for variable interest rate exposure is 52% for 2016/2017, 54% for 2017/2018 and 56% for 2018/2019 of net outstanding principal sums.

18. All loans and investments are at fixed rates of interest.

TrI 5 – Maturity Structure of Borrowing

Limits on the Maturity Structure of Borrowing	**Upper Limit**	**Lower Limit**	**Actuals 2016/2017 Next Call Date**	**Actuals 2016/2017 Contracted Maturity**
Maturity Period:				
Under 12 months	25%	0%	13.0%	3.0%
12 months and within 24 months	25%	0%	4.4%	4.4%
2 years and within 5 years	45%	0%	8.3%	6.5%
5 years and within 10 years	75%	0%	14.2%	14.2%
10 years and above	100%	0%	60.1%	71.9%

19. In addition to the main maturity indicators it is considered prudent that no more than 15% of long term loans should fall due for repayment within any one financial year. Using CIPFAs guidance notes, it is recommended that treasury reports show LOBOs at the next call date, however, the Code states that LOBOs should be shown in the accounts disclosure notes when “the counterparty could first require payment”. This would ordinarily be the maturity date (further details are shown in Appendix C(i)).

20. Applying the CIPFA recommendation, for the treasury report, the actual maximum percentage falling due for repayment in any one year is currently 13.2% (£44million) in 2017/2018. Through call options, the lender has the right to change the interest rate at various points, in which case the Council will repay

the loans and consider whether it needs to refinance them. In the current economic climate (where interest rates are expected to remain low for some time) they are extremely unlikely to be called.

TrI 6 – Total Principal Sums invested for periods longer than 364 days

21. This TrI is covered by the Annual Investment Strategy, which is detailed in Appendix B.

Other Treasury Management issues

Short Term Cash Deficits and Surpluses

22. It was agreed, as per the approved Strategy, that temporary loans and deposits would be used to cover short term cash surpluses and deficits that arise during the year. Such borrowing or investments would be made to specific dates at fixed rates, with reference to cash flow requirements. Investments have also been placed in Money Market Funds during the year.

23. All outstanding deposits are summarised in Appendix C (ii).

Icelandic Bank Deposits

24. Nothing further to report.

Longer Term Cash Balances

25. The average interest rate on present long-term debt is 3.771%, which continues to be relatively low when compared with other local authority borrowing rates.

26. Interest rate movements in the financial year have not provided many opportunities for an increased return through longer term investment of the more permanent cash surpluses, such as reserves and balances. The tight monetary conditions have continued through 2016/2017 without much upward movement in the deposit rates for all types of investments (short/medium and long term). As a result opportunities for an increased return by longer term investment of the more permanent cash surpluses, such as reserves and balances have been limited.

APPENDIX B

REVIEW OF INVESTMENT STRATEGY FOR 2016/2017

1. All investments of surplus cash balances were placed to ensure:

    a) the security of capital, deposits only being placed with financial institutions which met the high credit ratings laid down in the approved Strategy;

    b) the liquidity of investments, all deposits being placed for fixed periods at fixed rates of interest; and

    c) all such investments were in sterling and in “Specified Investments”, as prescribed in the DCLG Guidance on Local Government Investments (the “Guidance”).

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

3. Details of the deposits outstanding at the end of the year, totalling £57.582 million, are shown in Appendix C (ii). These deposits represent the Council’s reserves both long term, such as the PFI and Insurance funds, and short term such as creditors or payments in advance.

4. Subject to the cash position, available opportunities to invest in longer term investments, up to 12 months, were taken during the year, taking advantage of marginally higher interest rates available for the longer maturity period, where appropriate and within the minimum requirements set out in the Treasury Strategy. These are shown within general deposits in Appendix C (ii).

5. The Council contracts with a treasury adviser, regularly reviewing credit ratings of potential organisations and their respective country's ratings, together with other 'tools' used to assess the credit quality of institutions such as credit default swaps. The Council uses this information to assess institutions with which it may place deposits or from which it may borrow, including interest rate forecasts for both borrowing and investment, together with setting a 'benchmark' borrowing rate. The Council's investment policy is 'aimed' at the prudent investment of surplus cash balances to optimise returns whilst ensuring the security of capital and liquidity of investments. However, the Council, like any other organisation, can be exposed to financial risk, which is negated as far as possible by the aforementioned measures.

Appendix C (i)

SUMMARY OF BORROWING AND INVESTMENTS 2016/2017

Summary of Long Term Borrowing 2016/2017

Maturity Profile of Borrowing at 31 March 2017

Year	Amount (£m)					Percentage of Fund (%)		Average Rate (%)	
	PWLB	Market Loans (LOBOS)		Total					
		Next Call Date	Contracted Maturity	Next Call Date	Contracted Maturity	Next Call Date	Contracted Maturity	Next Call Date	Contracted Maturity
	(A)	(B)	(C)	(A) + (B)	(A) + (C)				
0 – 5	54.810	40.000		94.810	54.810	28.1	16.2	3.30	2.47
6 – 15	92.623			92.623	92.623	27.4	27.4	3.51	3.51
16 – 25	64.000			64.000	64.000	18.9	18.9	3.94	3.94
26 – 50	65.500	15.000	51.000	80.500	120.500	23.8	35.7	4.46	4.45
Over 50	0.000	6.000	10.000	6.000	6.000	1.8	1.8	4.21	4.21
Totals	**276.933**	**61.000**	**61.000**	**337.933**	**337.933**	**100.0**	**100.0**	**3.77**	**3.77**

Average Period to Maturity (Years)	**20.11**	**22.37**

The CIPFA Guidance Notes on Treasury Management in the Public Services recommends that the Treasury Management Strategy Reports include LOBO loans (Lender Option Borrower Option) at the earliest date on which the lender can require payment, deemed to be the next ‘call date’. At that date the lender may choose to increase the interest rate and the borrower (the Council) may accept the new rate or repay the loan (under the current approved Treasury Management Strategy, the Council would repay the loan). Whether or not the lender chooses to exercise their right to alter the interest rate will depend on market conditions. Current market conditions, where interest rates are predicted to remain low for some time, indicate that it is highly unlikely that lenders will call the loans in the immediate future.

The alternative method of determining the maturity profile of LOBO loans, based on contracted maturity, is used in the 2016/2017 Statement of Accounts.

The table above includes the maturity profiles using both the earliest date on which the lender can require payment and the contracted maturity dates.

Summary of Deposits 2016/2017

Deposits Outstanding at 31 March 2017

Borrower	Amount £m	Terms	Interest Rate (%)	Capita Credit Rating
Barclays	8.000	Fixed to 18/04/2017	0.25	Red – 6 months
Lloyds	5.000	Fixed to 18/04/2017	0.45	Red – 6 months
Nationwide BS	8.000	Fixed to 03/07/2017	0.36	Red – 6 months
National Bank of Qatar	8.000	Fixed to 14/08/2017	0.66	Orange – 12 months
Bank of Abu Dhabi	8.000	Fixed to 14/09/2017	0.48	Orange – 12 months
DBS Bank	8.000	Fixed to 18/09/2017	0.43	Orange – 12 months
HSBC	0.900	Overnight	0.10	Orange – 12 months
Ignis MMF	11.662	No fixed maturity date	0.28	AAA
Various MMFs	0.020	No fixed maturity date	0.21-0.27	AAA
Total	**57.582**			

Investments held have decreased by £20.0million between the end of December 2016 (as reported in the previous quarter end report) and the end of March 2017. This is due to changes in cashflows (decreased receipts/increased payments) and the repayment of a PWLB loan for £10million which was not refinanced.

The cash position is constantly reviewed to ensure that the Council maintains an appropriate level for daily cashflow purposes. The differences in investment levels as the year progressed is shown in the table below.

	31/03/16 £m	30/06/16 £m	Change £m	30/09/16 £m	Change £m	31/12/16 £m	Change £m	31/03/17 £m	Change £m
Total Deposits Oustanding	27.371	56.250	28.879	58.314	2.064	77.572	19.258	57.582	-19.990

Temporary Loans Outstanding at 31 March 2017

There were no temporary loans outstanding at the end of 2016/2017.