Title of Report:	**Treasury Management Annual Report 2014/15**
Report to be considered by:	Executive on 10 September 2015
Forward Plan Ref:	EX3016

Purpose of Report: **To inform Members of the treasury management activity and performance of the Council's investments for the financial year 2014/15.**

Recommended Action: **To note the previous year's treasury management activities and performance of the fund.**

Reason for decision to be taken: To ensure compliance with the updated CIPFA Code of Practice for Treasury Management in the Public Services 2009 and in accordance with Best Practice.

Other options considered: N/A

Key background documentation:
Treasury Management in the Public Services: Code of Practice 2009
Annual Investment Strategy 2014/15
Annual Investment Strategy 2015/16
Capital Strategy and Programme 2014-2019
Capital Strategy and Programme 2015-2020
MTFS 2014-2017
MTFS 2015-2018

The proposals will help achieve the following Council Strategy aim:

☐ **MEC – Become an even more effective Council**
☐ **MEC1 – Become an even more effective Council**

The proposals contained in this report will help to achieve the above Council Strategy principle by:
Detailing the activity of the Treasury management function and the contribution it makes to the Council's annual budget at minimum risk to the security of the monies invested.

Portfolio Member Details	
Name & Telephone No.:	Councillor Roger Croft
E-mail Address:	Rcroft@westberks.gov.uk
Date Portfolio Member agreed report:	4th August 2015

Contact Officer Details	
Name:	Gabrielle Esplin
Job Title:	Finance Manager
Tel. No.:	01635 519836
E-mail Address:	gesplin@westberks.gov.uk

Implications

Policy:	The Council's cash flow, borrowing and investments are carried out in accordance with the Annual Investment Strategy agreed by Council, March 2015
Financial:	The Treasury function is responsible for the daily cash flow management of the Council. Investment income generated from the Treasury Management contributes to the Council's annual budget.
Personnel:	None
Legal/Procurement:	None
Property:	None
Risk Management:	All investments are undertaken with a view to minimising risk and exposure to loss. The Treasury Management Strategy approved by the Council in March 2015 sets parameters to ensure this.
Corporate Board's Recommendation:	That the report be considered by Management Board.

Is this item relevant to equality? Please tick relevant boxes	**Yes**	**No**
Does the policy affect service users, employees or the wider community and:		
• Is it likely to affect people with particular protected characteristics differently?	☐	☒
• Is it a major policy, significantly affecting how functions are delivered?	☐	☒
• Will the policy have a significant impact on how other organisations operate in terms of equality?	☐	☒
• Does the policy relate to functions that engagement has identified as being important to people with particular protected characteristics?	☐	☒
• Does the policy relate to an area with known inequalities?	☐	☒
Outcome (Where one or more 'Yes' boxes are ticked, the item is relevant to equality)		
Relevant to equality - Complete an EIA available at www.westberks.gov.uk/eia		☐
Not relevant to equality		☒

Is this item subject to call-in?	Yes: ☐	No: ☒
If not subject to call-in please put a cross in the appropriate box:		
The item is due to be referred to Council for final approval		☐
Delays in implementation could have serious financial implications for the Council		☐
Delays in implementation could compromise the Council's position		☐
Considered or reviewed by Overview and Scrutiny Management Commission or associated Task Groups within preceding six months		☐
Item is Urgent Key Decision		☐
Report is to note only		☒

Executive Summary

1 Introduction

1.1 The aim of the Council's Treasury Management Strategy is to manage cash flow to ensure sufficient funds are available on a day to day basis for the Council's operations. Any surplus funds are invested to generate the most interest, while minimising the exposure of investments to risk. Investment and borrowing activities in 2014/15, were set against an economic context of slow growth and very low inflation and interest rates.

2 Summary of Findings

2.1 The average level of funds invested by the Council in 2014/15 (net of short term borrowing) was £12.7 million. Funds were invested in instant access deposit accounts with Natwest, Bank of Scotland, and the Goldman Sachs Global Liquidity money market fund, which paid rates of interest of up to 0.43%; a deposit account with Santander UK which paid 0.8% in 2014/15 but is now reduced to 0.4%; and fixed term deposits with UK Building Societies for an average period of 42 days and an average rates of 0.55%. The maximum amount invested with any one institution was £5 million. A number of short term loans were also arranged from other Local Authorities to cover our short term cashflow needs. The average length of loan was 12 days and the average rate of interest paid was 0.41%.

2.2 The Council earned total interest on its investments (net of interest paid on short term borrowing) of £93,000 or 0.73% of the average fund value. We also received a discount of 3.1% or £298,000 on our contributions to the Berkshire Pension Fund, by paying the contributions in advance. Taking into account this saving, the total net amount earned through cashflow management was £391,000 (compared with the budget for interest on investments of £378,000). If we include the gain on early payment of pension contributions, this would represent a return of around 2.2%.

2.3 £17.7 million new longer term loans were also taken from the Public Works and Loans Board (PWLB) to fund capital expenditure in 2014/15 and earlier years. The loans were for between 5 years at 1.5% interest and 40 years at 3.21%, with the length of loan linked to the estimated useful life of the asset funded. £3.4 million repayments were made on existing capital financing loans, bringing the Council's total long term capital financing debt with the PWLB to £115.7 million.

3 Equalities Impact Assessment

3.1 This item is not relevant to equality.

4 Conclusion

4.1 The Treasury Management Group (including the Portfolio Holder for Finance) will monitor and review the Council's investments and borrowing during 2015/16, to ensure that treasury activities continue in line with the approved Treasury Management Strategy in order to ensure the security and liquidity of and return on the Councils funds. The group will also aim to finance the Council's Capital Programme at the best available rates of interest.

Executive Report

1. Introduction

1.1. The CIPFA Code of Practice for Treasury Management in the Public Services, revised in April 2009, requires the Section 151 Officer to provide annual reports to the Executive before the start of the financial year and after the year end. Before the start of the financial year, the strategy and plan to be pursued in the forthcoming year is reported. After the close of the financial year, an annual report reviewing the Treasury Management activity and performance for the previous year is provided.

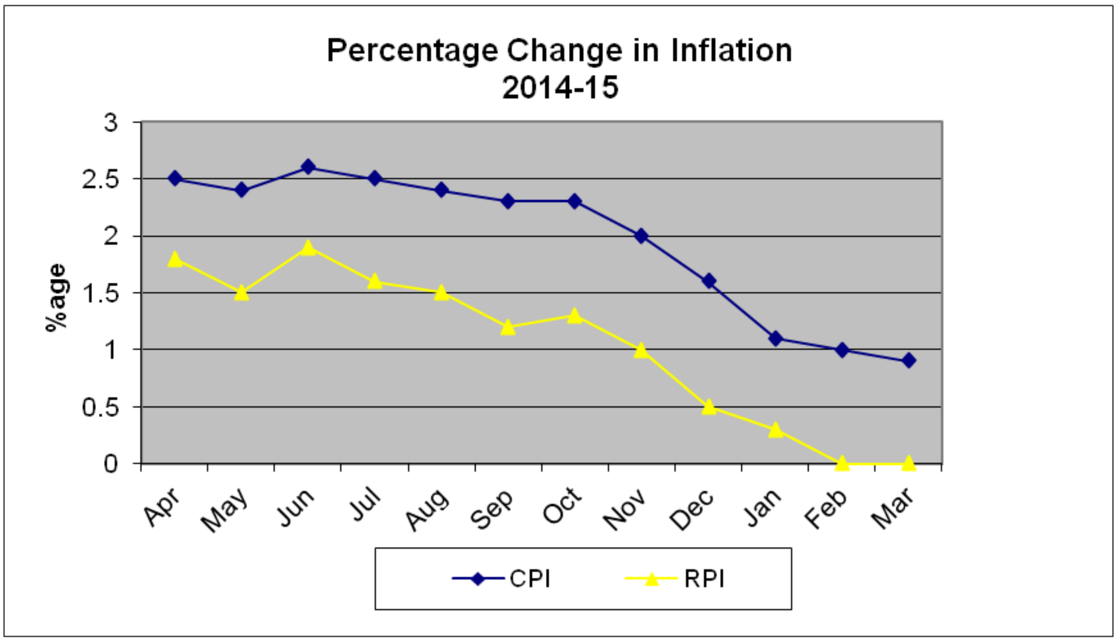
1.2. The aim of the latest investment strategy, which was approved by the Council in March 2015, is to manage the Council's cash flow to ensure sufficient funds are available on a day to day basis for the Council's operations. Any surplus funds are invested to generate the most beneficial interest receipts, while minimising the exposure of investments to risk.

1.3. In 2014/15 the Treasury Management Group met three times to review performance and determine the detail of policy. This group consists of the Head of Finance, the Chief Accountant, the Finance Manager for Capital, Assets, VAT and Treasury, the Treasury Accountant, the Portfolio Member for Finance and two other members.

2. Economic conditions

2.1 The government's main measure of inflation, which the Bank of England Monetary Policy Committee (MPC) uses to inform its interest rate decisions, is the Consumer Price Index (CPI). Annual CPI fell below the Bank of England 2% target during 2014/15 (Chart 1) and reached 0% at the end of March. The main factors driving down CPI were reduced food and energy prices. The MPC's current policy aim is for inflation to return to the 2% target within 2 years.

Chart 1



2.2 The latest Bank of England inflation report (May 2015) states that the GDP growth was robust in 2014, moderating in the second half of the year. Despite the weakness in the first quarter of 2015, the outlook for growth remains solid. Household real incomes have been boosted by the fall in food, energy and imported goods prices. The absorption of remaining slack and a pickup in productivity growth are expected to support wage growth in the period ahead. Along with the low cost of finance, that will help maintain domestic demand growth.

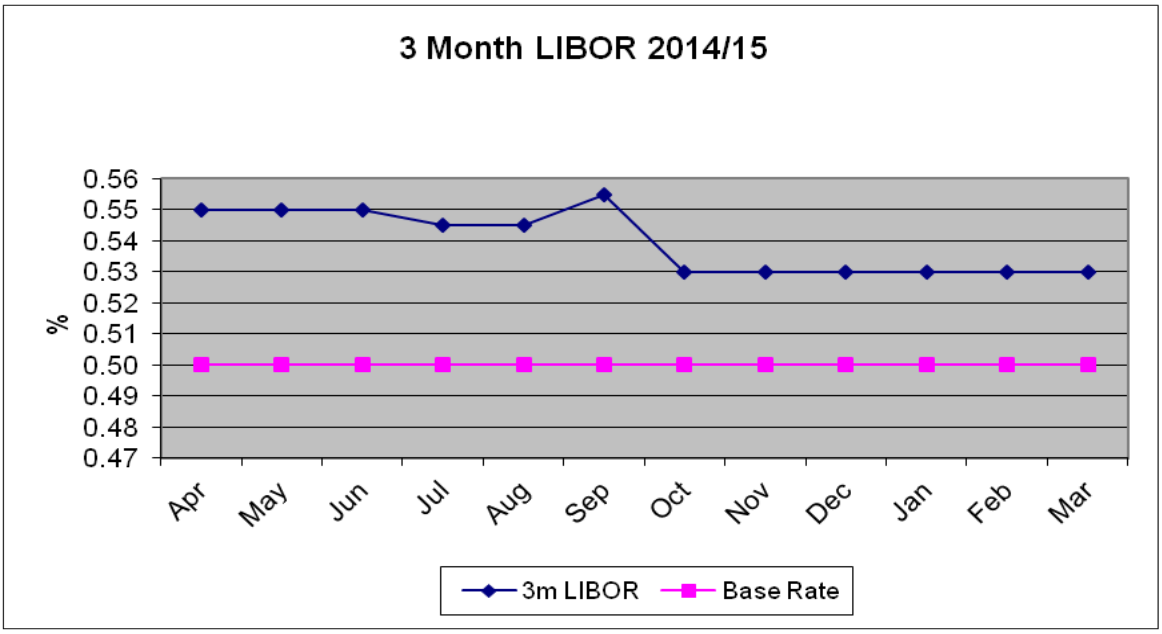
2.3 A combination of very weak pay rises and inflation above the rate of pay rises meant that consumer disposable income was still being eroded and expectations for the first increase in Bank Rate therefore started to recede as growth was still heavily dependent on better consumer demand.

2.4 Official interest rates in the United Kingdom remained at historically low levels with the Bank of England base rate at 0.50% for the sixth consecutive year. The European Central Bank announced details of an expanded asset purchase programme. Short and long-term interest rates fell across many advanced economies.

2.5 During the second half of 2014 financial markets were caught out by a halving of the oil prices. The Bank and HM Treasury announced an amendment to the Funding for lending Scheme (FLS) on 2 December 2014 which allows participants to borrow from the FLS until January 2016, with incentives to boost lending to small and medium sized enterprises (SMEs).

2.6 The rates available to the Council reflect the three month sterling London Inter-Bank Offer Rate or LIBOR (this is the rate at which the banks are prepared to lend to each other). LIBOR (see Chart 2) has remained fairly flat throughout the year starting year at 0.55% with a slight improvement to nearly 0.56% in September before levelling down to 0.53% for the latter part of year. The overall level is still an improvement on the average level of 2013/14 0.51%.

<u>Chart2</u>



2.7 Interest rates offered by banks and building societies continue to be low for Local Authorities. WBC received notifications of reductions in deposit rates from its NatWest and Santander UK.call accounts.

2.8 Despite these pressures, there was a slight improvement in the interest rates earned by the Council over the course of 2014/15 with reasonable returns on investments made for 3 months or more although with the base rate and economy static there were no sudden surges in rates.

3 Overview of Cash Flow and Treasury Management Strategy

3.1 Guidance on Local Government Investments in England gives priority to security and liquidity. The Council's Treasury Management Strategy therefore aims to maximise the return on its investments without compromising these principles. The Council manages all its investments and borrowing in house.

3.2 The amount of cash held by the Council fluctuates throughout the year and within each month, depending on the dates on which major government grants are received and when large payments are made - in particular, weekly creditors payments and monthly salaries. In general terms, funds are high on the first working day of the month when a large proportion of Council tax and government grant is received and low on the last working day of the month when the majority of staff salaries are paid. The Council's overall funds are lower at the end of the financial year, because most Council Tax is paid over ten months from April to January.

3.3 It should be borne in mind that the amount of cash held by the Council does not equate to the total usable reserves shown on the Council's balance sheet. This is because we have chosen to minimise the amount borrowed to fund capital expenditure, by offsetting our borrowing needs against our reserves. This is in order to minimise the revenue cost of borrowing and to avoid the risks associated with investing large balances.

4 Short Term Investments and Borrowing in 2014/15

4.1 In order to ensure that the Council's day to day cash flow requirements can be met a sum of between approximately £1 million and £20 million is held in instant access accounts. Table 1 shows the institutions and interest rates for these accounts:

Table 1

Institution:	Interest Rate:	Changing to:
Bank of Scotland	0.40%	No change
NatWest	0.25% < £500K/0.40% > £500K	0.25% overall from May 2015
Santander UK	0.80%	0.40% from July 2015
Goldman Sachs Money Market Fund	Variable averaging 0.40%	Latest rates 0.43%

4.2 In accordance with the Council's Treasury Management Strategy, the deposit accounts are held with banks rated A by the Fitch Credit Ratings Agency, while the money market fund is rated AAA by Fitch (these ratings indicate a very low risk of default on investments). The maximum held in each account at any one time was £5 million.

4.3 At various points in the year the Council had surplus funds which it placed in fixed term, fixed rate investments until they were needed to cover outgoings. The longer the term of the investment, the higher the rate of interest earned. During the year, 28 fixed term investments were made for periods of between 1 day and 364 days. All these investments were placed with the top 20 British Building Societies. The maximum invested with any one institution was £5 million, with lower limits on the amounts invested with the smaller building societies. The average length of investment was 41 days and the average interest earned on these investments was 0.77%.

4.4 The majority of the Council's investments are arranged through one of five firms of financial brokers, which have ready access to the most competitive interest rates on the market each day.

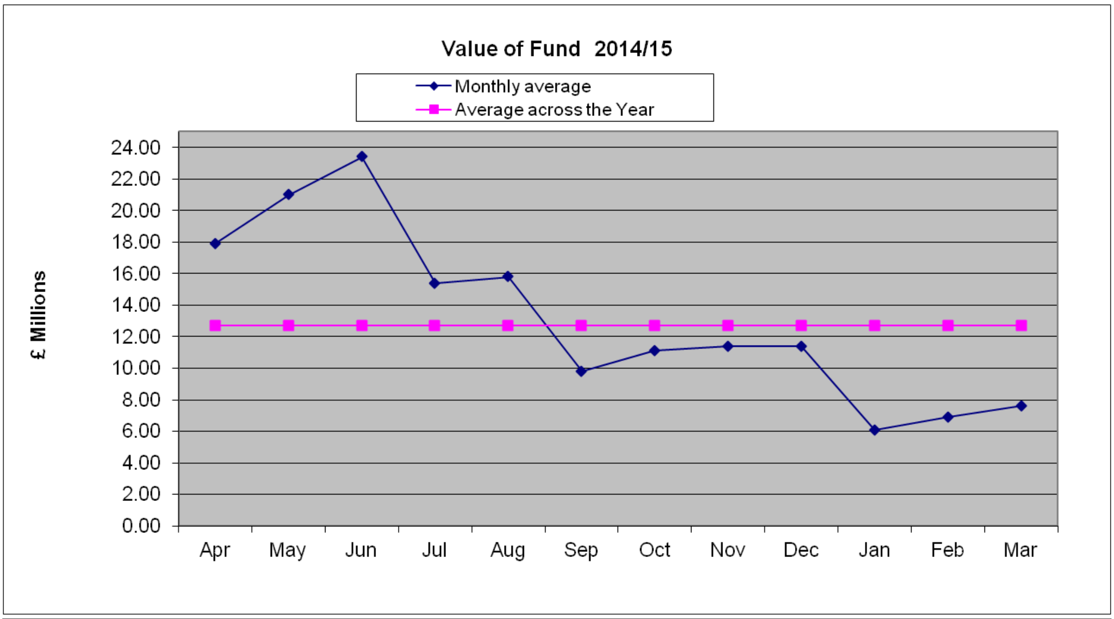
4.5 It was also necessary from time to time for the Council to take out short term loans to cover its cash flow requirements. 32 short term loans were taken out during the financial year, all from other local authorities, for periods of between 1 day and 62 days, at rates of interest between 0.27% and 0.50%. 23 of these loans were for 15 days or less. The average length of loan was 9 days and the average interest paid on these loans was 0.41%.

4.6 In addition, some short term borrowing was undertaken to finance capital expenditure on an interim basis, in order to take advantage of cheap short term borrowing rates. The Council had loans of £6 million from Derbyshire County Council for this purpose between April and October 2014 at an average rate of 0.51%.. This was refinanced through a longer term loan from the Public Works and Loans Board (PWLB) in October 2014. We also took at a loan of £2 million from Oxford City Council from December 2014 to September 2015 at a rate of 0.62% which we also plan to refinance through a longer term PWLB loan in 2015/16.

5 Overall Performance of the Treasury Fund

5.1 The average value of the fund during the year (i.e. the total of temporary investments less temporary borrowing) was £12.7 million (see Chart 3). The net value of the fund at 31st March 2015 was -£2.4 million on the 31st March 2015 because of the need to borrow to cover payroll and creditors on the last day of the year.

Chart 3



5.2 The net amount of interest earned from the Council's investment and short term borrowing activities in 2014/15 was £93,000 compared with £97,000 in 2013/14. This represents a net rate of return of 0.73% as compared with the average bank base rate for the year of 0.50%.

5.3 In addition, the Royal Borough of Windsor and Maidenhead, who manage the Berkshire pension fund , offered West Berkshire a discount of 3.10% on its total pension contributions due for the year in exchange for paying the contributions in advance in April 2014 instead of in monthly instalments. In this way, the Council achieved a saving of £298,000, by, in effect, making a temporary investment of approximately £10.7 million with the Berkshire Pension Fund at a rate of return of 3.10%. This was achieved because the Pension Fund is much bigger than the West Berkshire treasury fund and is able to invest over longer periods and therefore to earn a higher rate of return. Taking into account this saving, therefore, the total net investment income earned was £391,000. This compares favourably with the 2014/15 budget for interest on investments of £378,000.

5.4 If the average fund balance is adjusted to include the average level prepaid pension contributions (approximately £5.2m across the year), and if the saving achieved through this arrangement is included in our return on investments, the overall rate of return would equate to 2.2%.

5.5 Table 2 (below) shows that investment and borrowing activities in 2014/15 were largely in line with the Treasury Management Strategy approved by Council in March and with the more detailed Treasury Management Policies, which underpin the Strategy. There were a few exceptional circumstances when unexpected payments were received into or paid out of the Council's main bank account. In these cases the account was returned to its approved limit on the next working day.

Table 2

Policy	Target	Actual	Explanation
Credit limit with counterparties not exceeded	100%	96.05%	Late clearing of receipts into the Council's main bank account meant that on 10 out of 253 working days the £5 million counterparty limit with Natwest was exceeded. On all occasions, this was corrected the next working day.
All counterparties on approved lending list	100%	100%	
All investments are approved investments	100%	100%	
Segregation of duties complied with	100%	100%	
Current account daily balance within +/- £100k of estimate	100%	99.9%	Natwest SIBA automatically ensures a credit £10K balance unless we overdraw. The normal maximum overdraft of £100,000 was exceeded on 1 occasion when the Treasury team were not informed in time of large urgent payments to be made.
Target for short term debt of £15m not exceeded	100%	100%	There were no occasions where this target was breached

6 Long Term Borrowing in 2014/15

6.1 With the exception of debt embedded in the PFI contract, all the Council's long term debt is with the Public Works and Loans Board (PWLB). The level of long term borrowing in 2014/15 was in line with the prudential borrowing limits set out in the Annual Investment Strategy 2014/15 and the Capital Strategy 2014-2019, which were both approved by the Council in March 2014. Borrowing needs were also reviewed during the year by the Treasury Management Group.

6.2 At 1 April 2014 the Council had long term PWLB loans of £101.4 million (including £20.6 million remaining from the loans inherited from the former Berkshire County Council). During 2015/16 new PWLB loans of £17.7 million were taken out as follows:

Table 3

New PWLB Loans 2014/15	Amount	Type	Rate
To fund capital expenditure prior to 2010 previously offset against internal balances (including refinancing of interim loan from Derbyshire County Council – see paragraph 4.6)	£8,000,000	Annuity	3.80%
Capital spend in 2015/16 on assets with 5 year life (including highways maintenance	£600,000	Annuity	1.50%
Capital spend in 2015/16 on assets with 10 year life (including highways maintenance)	£3,400,000	Annuity	1.99%
Capital spend in 2015/16 on assets with 25 year life (including highways improvements and building maintenance)	£2,200,000	Annuity	2.81%
Capital spend in 2015/16 assets with 40 year life (mainly new buildings, including schools)	£3,500,000	Annuity	3.21%

6.3 £3.4 million loan repayments were made in 2014/15, leaving the balance of long term debt with the PWLB at 31st March 2015 at £115.7million.

6.4 In the current financial year (2015/16) we anticipate that the Council's total long term PWLB debt will increase by approximately £9.3 million, to £125.0m to allow for the financing of planned capital expenditure in 2015/16 and previous years less principal repayments due to be made this year on existing loans. Over the next six years, the level of the Council's long term debt is expected to reach a peak of approximately £145 million. This debt level is in line with the capital strategy and MTFS approved by Council in March 2015. From 2021/22 onwards, the Council's long term debt is expected to start to decrease at a rate of about £1.5m per year.

6.5 These figures do not include the debt embedded in the Waste PFI contract to finance the cost of building the Padworth Waste Management facility. This debt, which is included in the total borrowing shown on the Council's balance sheet, stood at £16 million at the 31st March 2015. (Repayments of this debt are included in the monthly waste contract charges, which are paid from the revenue budget for waste management).

6.6 As explained in paragraph 3.3 (above), the Council has avoided borrowing more than is necessary in the past, by offsetting some capital expenditure against its useable reserves. This means that, if the Council wishes to spend any significant amount from its reserves, it is likely to be necessary to undertake more borrowing to refinance previous years' capital expenditure, so increasing the revenue cost of financing capital spend. However, the forecast future level of borrowing and the cost of debt repayments included in the MTFS both allow for the amount expected to be borrowed to refinance previous year's capital expenditure.

6.7 The council also aims to minimise borrowing by making use of capital receipts wherever possible to fund capital investment.

Appendices

There are no Appendices to this report.

Consultees

Local Stakeholders:	Treasury Management Group
Officers Consulted:	None
Trade Union:	None