

FAREHAM

BOROUGH COUNCIL

Report to the Executive for Decision 11 July 2016

Portfolio:	Policy and Resources
Subject:	Capital and Treasury Management Outturn 2015/16
Report of:	Director of Finance and Resources
Strategy/Policy:	Finance Strategy
Corporate Objective:	A dynamic, prudent and progressive Council

Purpose:

This report provides the Executive with details of the capital and treasury management outturn for 2015/16 to comply with the reporting requirements of the Code of Practice for Treasury Management. The report also seeks approval for the proposed methods of financing the General Fund capital programme.

Executive summary:

Actual capital expenditure on General Fund schemes in 2015/16 was £17,259,729 compared with the revised capital programme of £20,911,100. The overall variance was £3,651,371 and a detailed analysis of the variations is given in Appendix A to the report.

Total savings of £126,200 were achieved, additional expenditure of £12,657 was incurred and a total of £3,537,828 will be carried forward into 2016/17.

Details of the various methods used to finance this expenditure are set out in Appendix A to the report.

Full details of investment and borrowing activity in 2015/16 are set out in the main body of this report. Investment activity in 2015/16 is summarised below:

	£m
Investments as at 1 April 2015	43.1
Investments made in 2015/16	163.8
Investments repaid in 2015/16	174.1
Investments as at 31 March 2016	32.8

Total external investment interest received for the year was £381,912. The total of external interest paid on borrowing and other amounts invested with the Council was £1,404,922.

The net total of £1,023,010 has been allocated to the Council's funds as shown in the following table:

	£
General Fund	703,260
Housing Revenue Account	(1,727,664)
Whiteley Fund	1,394
Total External Interest	(1,023,010)

During 2015/16, the Council complied with its legislative and regulatory requirements of the Prudential Code.

Recommendation:

That the Executive agrees;

- (a) the General Fund capital programme for 2015/16 be approved and financed as set out in Appendix A to this report;
- (b) the additional expenditure incurred, amounting to £12,657 be financed retrospectively from surplus capital resources; and
- (c) the actual General Fund capital expenditure and treasury management activity for 2015/16 be noted.

Reason:

To provide the Executive with details of the capital and treasury management outturn in 2015/16 and to comply with the reporting requirements of the Code of Practice for Treasury Management.

Cost of proposals:

The necessary resources are available to finance the General Fund capital programme for 2015/16 including the additional expenditure of £12,657.

Appendices:

- A:** Capital Expenditure and Financing 2015/16
- B:** Economic Commentary by Treasury Advisors, Arlingclose
- C:** Total Investment Activity 2015/16
- D:** Prudential and Treasury Indicators 2015/16

Background papers: None

Reference papers: CIPFA Code of Practice for Treasury Management

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BOROUGH COUNCIL

Executive Briefing Paper

Date:	11 July 2016
Subject:	Capital and Treasury Management Outturn 2015/16
Briefing by:	Director of Finance and Resources
Portfolio:	Policy and Resources

INTRODUCTION

1. This report provides the Executive with details of the capital and treasury management outturn for 2015/16 to comply with the reporting requirements of the Code of Practice for Treasury Management.

CAPITAL

2. The capital programme for 2015/16, approved in February this year for the General Fund was £20,911,100. The actual capital expenditure, detailed in Appendix A, was £17,259,729 giving an overall variation of £3,651,371. A summary, including savings and additional expenditure, is summarised in the table below.

	Revised Budget £	Actual £	Savings £	Additional Expend £	Carry forward £
Streetscene	47,900	9,902	0	1,626	39,624
Planning & Development	31,700	9,727	0	0	21,973
Leisure & Community	8,256,900	5,536,846	71,782	1,635	2,649,907
Health & Housing	1,630,400	1,239,617	3,730	9,396	396,449
Policy & Resources	10,944,200	10,463,637	50,688	0	429,875
Total	20,911,100	17,259,729	126,200	12,657	3,537,828

SAVINGS AND ADDITIONAL EXPENDITURE

3. In the year there were a number of schemes that were completed at a lower cost than originally anticipated. The savings for the year totalled £126,200.
4. The main areas for savings were £48,072 on Play and Parks Schemes, £23,710 on Outdoor Recreation Schemes and £50,688 on Commercial Property Investment Acquisitions.

CARRY FORWARDS TO 2016/17

5. There are a number of schemes still in progress and a total budget of £3,537,828 will be carried forward to 2016/17. An explanation for the larger carry forwards are set out in the following paragraphs.

STREETSCENE

6. The Street Lighting underspend of £39,624 will be carried forward for 2016/17 to fund the maintenance of the street lights at Market Quay roundabout.

LEISURE AND COMMUNITY

7. Construction is progressing well at Holly Hill Leisure Centre and the centre will open in September 2016. The remaining budget of £2,527,122 for 2015/16 will be carried forward into 2016/17. The project is currently targeted to complete within 1% of the approved budget, although the final account is likely to be subject to considerable dialogue between the Council and the contractor.
8. Works to extend Blackbrook Play Area completed in early 2016/17. The £40,000 budget will be carried forward to match the expenditure.
9. The conversion of the Park Lane Tennis Courts into additional car parking was also completed in early 2016/17. The remaining £54,000 budget will be carried forward to match the expenditure.

HEALTH AND HOUSING

10. The unspent budget for land acquisitions for enabling schemes relates to property in Gosport Road. The unspent budget of £360,000 will be carried forward into 2016/17.

POLICY AND RESOURCES

11. The underspends on the Vehicles and Plant and ICT rolling programmes totalling £305,374 will be carried forward to fund the proposed spending plans in 2016/17.
12. The carry forward of £150,223 for the Civic Offices will be used to fund future improvement works in 2016/17.
13. For the Daedalus Development, legal and professional costs were incurred earlier than anticipated for some of the major projects, including the new hangars. The overspend of £49,153 will be carried forward and offset against the 2016/17 budget.

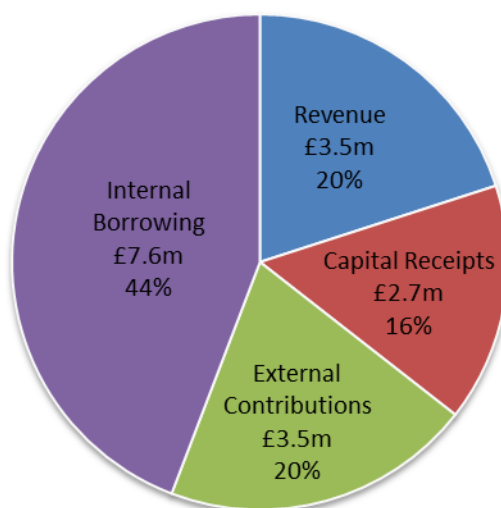
CAPITAL PROGRAMME 2016/17 TO 2020/21

14. The General Fund capital programme will be reviewed by officers in light of the slippage and re-phasing of works and an updated programme for 2016/17 to 2020/21 will be presented to the Executive as part of the Finance Strategy for 2017/18.

CAPITAL FINANCING

15. Details of the various methods used to finance the capital expenditure in 2015/16 are set out in Appendix A. External funding contributed to 20% of the Council's capital programme as shown in the chart below.

Capital Financing



TREASURY MANAGEMENT

16. The Chartered Institute of Public Finance and Accountancy's Treasury Management Code (CIPFA's TM Code) requires the Council to report on the performance of the treasury management function at least twice a year (mid-year and at year end).
17. The Council's Treasury Management Strategy 2015/16 was approved by full Council on 23 April 2015.
18. The Council has invested large sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. This section of the report covers treasury activity and the associated monitoring and control of risk.
19. In April 2016, the Council changed Treasury Advisor from Capita Asset Services to Arlingclose. An economic commentary by Arlingclose can be found in Appendix B.

BORROWING ACTIVITY

20. At 31 March 2016 the Council held £44.8 million of loans, (an increase of £3 million on 31 March 2015).
21. The Council's main objective when borrowing is to strike a low risk balance between securing low interest rates and achieving cost certainty over the period for which the funds are required.
22. Affordability and the 'cost of carry' remain important influences on the Council's borrowing strategy alongside the consideration that, any borrowing undertaken ahead of need, would have to be invested in the money markets at rates of interest significantly lower than the cost of borrowing. As short-term interest rates have remained and are likely to remain at least over the forthcoming two years, lower than long-term interest rates, the Council determined it was more cost effective in the short term to use internal resources (internal borrowing) and short-term loans instead.
23. The benefits of internal borrowing are monitored regularly against the potential for incurring

additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. The Council's treasury advisors assist with this 'cost of carry' and breakeven analysis.

24. Borrowing activity during the year was:

	Balance on 31 March 2015 £'000	Balance on 31 March 2016 £'000	Average Rate
Long Term Borrowing	40,000	40,000	3.50%
Temporary Borrowing	0	3,000	0.50%
Hampshire County Council	400	200	0.00%
Portchester Crematorium	1,091	1,333	0.25%
Charity of Winifred Nellie Cocks	285	286	0.50%
Total Borrowing	41,776	44,819	

25. The Council holds investments from Portchester Crematorium Joint Committee and the Charity of Miss Winifred Nellie Cocks which are treated as temporary loans.

INVESTMENT ACTIVITY

26. The Council holds large invested funds, representing income received in advance or expenditure plus balances and reserves held. During 2015/16 the Council's investment balances have ranged between £32.8 million and £49.3 million.
27. Guidance on Local Government Investments in England gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles.
28. Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2015/16.
29. A summary of investment activity during the year is shown in the table below.

	Externally Managed £m	Internally Managed £m	Call/Notice Accounts £m	Total £m
Investments at 1 April 2015	10.0	13.0	20.1	43.1
New investments	7.0	19.0	137.8	163.8
Investments repaid	7.0	12.0	155.1	174.1
Investments at 31 March 2016	10.0	20.0	2.8	32.8

30. The level of investment activity with each authorised institution is set out in Appendix C.
31. As the base rate has remained unchanged at 0.5% since March 2009, this has had a major impact on the rate of return on the Council's investments. The Council maintained an average balance of £45.7m of investments earning an average rate of return of 0.84% compared to the average 7-day LIBID rate of 0.36%.
32. The following table shows the range of interest rates for the investment portfolio at the end of the year compared with the position in the previous year:

	At 31 March 2015		At 31 March 2016	
	£m	%	£m	%
Interest Rate between 0.00% and 0.50%	10.1	23	2.8	9
Interest Rate between 0.51% and 1.00%	25.0	58	22.0	67
Interest Rate between 1.01% and 1.50%	8.0	19	6.0	18
Interest Rate between 1.51% and 2.00%	0.0	0	2.0	6
Total	43.1	100	32.8	100

INTEREST RECEIVED AND PAID

33. External interest received during the year was £381,912 which was allocated between the General Fund, the Housing Revenue Account (HRA) and the Whiteley Fund.
34. The allocation of interest to the HRA is based on the average balance for the year on the HRA, the Housing Repairs Account and the Major Repairs Reserve, using the average interest rate earned on external investments.
35. External interest paid during the year was £1,404,922 and was also allocated between the General Fund and the HRA. The amount payable by the HRA is made up of the interest payable on external PWLB loans, internal General Fund loan and the HRA capital financing requirement.
36. This calculation means that the amount payable by the HRA to the General Fund is actually greater than the external amount payable by the General Fund.
37. The overall net total of £1,023,010 has been allocated to the Council's funds as shown in the following table

	Interest Received £	Interest Paid £	Net Interest £
General Fund	251,627	451,633	703,260
Housing Revenue Account	128,891	(1,856,555)	(1,727,664)
Whiteley Fund	1,394	0	1,394
Total External Interest	381,912	(1,404,922)	(1,023,010)

38. The net balance credited to the General Fund was £703,260 against a revised budget of £699,900. The net balance debited to the HRA was £1,727,664 against a revised budget of £1,711,400.

COMMERCIAL PROPERTY INVESTMENT ACQUISITIONS

39. In January 2013, the Executive agreed £3 million to fund a commercial property investment acquisition programme as a means to optimise returns on Council investments. A further £5 million was agreed by the Executive in November 2013 and £8 million agreed in February 2016.
40. Two purchases were made during 2015/16. The total of commercial property investment acquisitions are as follows:

	Date of Purchase	Premises Type	Purchase Price £m
Clifton House, Segensworth	1 Aug 2013	Industrial	1,700
122-134 Seaside, Eastbourne	20 Dec 2013	Convenience Store	825
86-88 Mitcham Lane, Streatham	10 Mar 2014	Convenience Store	1,300
83 St Thomas St, Weymouth	29 Sept 2014	Retail	810
470 Ringwood Road, Poole	24 Nov 2014	Convenience Store	1,260
2 Armstrong Road, Oxford	20 Oct 2015	Nursery	1,890
136-138 Southampton Road, Park Gate	29 Feb 2016	Retail	7,628
Total			15,413

41. The seven premises will generate additional rental income of £1,053,500 per annum at a weighted average return of 7%.

PRUDENTIAL AND TREASURY INDICATORS

42. During 2015/16, the Council complied with its legislative and regulatory requirements. Appendix D shows the actual prudential and treasury indicators for 2015/16.

SUMMARY

43. This report gives details of General Fund capital and treasury management outturn in 2015/16 in accordance with the reporting requirements set out in the CIPFA Code of Practice for Treasury Management. Members of the Executive are asked to note the report.

RISK ASSESSMENT

44. There are no significant risk considerations in relation to this report.

Enquiries:

For further information on this report please contact Caroline Hancock. (Ext 4589)

APPENDIX A

CAPITAL EXPENDITURE 2015/16

	Budget £	Actual £	Savings £	Additional Expenditure £	Carry Forward £
STREETSCENE					
Health and Safety in Cemeteries	7,900	9,526		1,626	0
Street Lighting Maintenance	40,000	376			39,624
STREETSCENE TOTAL	47,900	9,902	0	1,626	39,624
PLANNING & DEVELOPMENT					
Osborn Road 5 Year Programme	21,700	2,842			18,858
Car Park Surface Improvements	10,000	6,885			3,115
PLANNING & DEVELOPMENT TOTAL	31,700	9,727	0	0	21,973
LEISURE & COMMUNITY					
Buildings					
Ferneham Hall Repairs	50,000	35,995			14,005
Review of Community Buildings	110,000	95,258			14,742
Holly Hill Leisure Centre	7,300,300	4,773,178			2,527,122
	7,460,300	4,904,431	0	0	2,555,869
Play and Parks Schemes					
Play Area Upgrades	50,000	30,634	19,366		0
Abshot Road Youth Facility	26,300	26,268	32		0
King George V	75,000	72,970	2,030		0
Park Lane Concrete Skate Park	28,000	28,388		388	0
Park Lane Outdoor Gym	30,000	30,252		252	0
Relocation of Play Area at Park Lane	83,000	83,400		400	0
Hammond Road Youth Facility	10,000	0	10,000		0
Segensworth Play Area	80,000	70,116	9,884		0
Stubbington Play Area	80,000	80,254		254	0
Course Park Play Area	40,000	38,240	1,760		0
Blackbrook Park Play Area	40,000	0			40,000
Birchen Road Play Area	50,000	45,000	5,000		0
	592,300	505,522	48,072	1,294	40,000
Outdoor Recreation Schemes					
Bath Lane Cricket Pavilion	83,000	83,341		341	0
Park Lane Tennis Courts	57,000	2,962			54,038
Stubbington Tennis Courts Refurbishment	19,300	527	18,773		0
Burridge Changing Rooms Improvements	15,000	10,063	4,937		0
	174,300	96,893	23,710	341	54,038
Grants to Community Groups					
Titchfield Amateur Boxing Club	25,000	25,000			0
Lee-on-the-Solent Golf Club	5,000	5,000			0
	30,000	30,000	0	0	0
LEISURE & COMMUNITY TOTAL	8,256,900	5,536,846	71,782	1,635	2,649,907

	Budget £	Actual £	Savings £	Additional Expenditure £	Carry Forward £
HEALTH & HOUSING					
Home Improvement Schemes					
Disabled Facilities Grants	480,000	489,388		9,388	0
Home Improvement Loans	80,000	53,395			26,605
Flood Repair and Renew Grants	6,300	6,308		8	0
	566,300	549,091	0	9,396	26,605
Enabling					
Land Acquisitions	1,040,000	676,270	3,730		360,000
Feasibility Studies	24,100	14,256			9,844
	1,064,100	690,526	3,730	0	369,844
HEALTH & HOUSING TOTAL	1,630,400	1,239,617	3,730	9,396	396,449
POLICY & RESOURCES					
Rolling Programmes					
Vehicles & Plant	428,600	212,473			216,127
ICT	271,000	181,753			89,247
	699,600	394,226	0	0	305,374
Council Buildings					
Depot Refurbishment	57,800	34,369			23,431
Civic Offices Improvements	200,000	49,777			150,223
	257,800	84,146	0	0	173,654
Other Schemes					
Commercial Property Investment Acquisitions	9,936,800	9,886,112	50,688		0
Daedalus Development	50,000	99,153			(49,153)
	9,986,800	9,985,265	50,688	0	(49,153)
POLICY & RESOURCES TOTAL	10,944,200	10,463,637	50,688	0	429,875
GENERAL FUND TOTAL	20,911,100	17,259,729	126,200	12,657	3,537,828

CAPITAL FINANCING 2015/16

	£
Revenue Resources:	
Direct Revenue Funding	449,014
Capital Fund Account	2,975,107
Matched Funding Reserve	30,000
Capital Receipts:	
Usable Capital Receipts	1,945,070
Capital Development Fund	739,566
External Contributions:	
Disabled Facilities Grant	330,978
HCA Grant	99,153
Repaid Renovation Grants	53,395
Community Infrastructure Levy	2,400,000
Leisure Developer Contributions	603,138
Environment Agency	6,308
Borrowing:	
Internal	7,628,000
Total Financing	17,259,729

ECONOMIC COMMENTARY BY TREASURY ADVISORS ARLINGCLOSE

Growth, Inflation, Employment: The UK economy slowed in 2015 with GDP growth falling to 2.3% from a robust 3.0% the year before. CPI inflation hovered around 0.0% through 2015 with deflationary spells in April, September and October. The prolonged spell of low inflation was attributed to the continued collapse in the price of oil from \$67 a barrel in May 2015 to just under \$28 a barrel in January 2016, the appreciation of sterling since 2013 pushing down import prices and weaker than anticipated wage growth resulting in subdued unit labour costs.

CPI picked up to 0.3% year/year in February, but this was still well below the Bank of England's 2% inflation target. The labour market continued to improve through 2015 and in Q1 2016, the latest figures (Jan 2016) showing the employment rate at 74.1% (the highest rate since comparable records began in 1971) and the unemployment rate at a 12 year low of 5.1%. Wage growth has however remained modest at around 2.2% excluding bonuses, but after a long period of negative real wage growth (i.e. after inflation) real earnings were positive and growing at their fastest rate in eight years, boosting consumers' spending power.

Global influences: The slowdown in the Chinese economy became the largest threat to the South East Asian region, particularly on economies with a large trade dependency on China and also to prospects for global growth as a whole. The effect of the Chinese authorities' intervention in their currency and equity markets was temporary and led to high market volatility as a consequence. There were falls in prices of equities and risky assets and a widening in corporate credit spreads.

As the global economy entered 2016 there was high uncertainty about growth, the outcome of the US presidential election and the consequences of June's referendum on whether the UK is to remain in the EU. Between February and March 2016 sterling had depreciated by around 3%, a significant proportion of the decline reflecting the uncertainty surrounding the referendum result.

UK Monetary Policy: The Bank of England's MPC (Monetary Policy Committee) made no change to policy, maintaining the Bank Rate at 0.5% (in March it entered its eighth year at 0.5%) and asset purchases (Quantitative Easing) at £375bn. In its *Inflation Reports* and monthly monetary policy meeting minutes, the Bank was at pains to stress and reiterate that when interest rates do begin to rise they were expected to do so more gradually and to a lower level than in recent cycles.

Improvement in household spending, business fixed investment, a strong housing sector and solid employment gains in the US allowed the Federal Reserve to raise rates in December 2015 for the first time in nine years to take the new Federal funds range to 0.25%-0.50%. Despite signalling four further rate hikes in 2016, the Fed chose not to increase rates further in Q1 and markets pared back expectations to no more than two further hikes this year.

However central bankers in the Eurozone, Switzerland, Sweden and Japan were forced to take policy rates into negative territory. The European Central Bank also announced a range of measures to inject sustained economic recovery and boost domestic inflation which included an increase in asset purchases (Quantitative Easing).

Market reaction: From June 2015 gilt yields were driven lower by the a weakening in

Chinese growth, the knock-on effects of the fall in its stock market, the continuing fall in the price of oil and commodities and acceptance of diminishing effectiveness of central bankers' unconventional policy actions. Added to this was the heightened uncertainty surrounding the outcome of the UK referendum on its continued membership of the EU as well as the US presidential elections which culminated in a significant volatility and in equities and corporate bond yields.

10-year gilt yields moved from 1.58% on 31/03/2015 to a high of 2.19% in June before falling back and ending the financial year at 1.42%. The pattern for 20-year gilts was similar, the yield rose from 2.15% in March 2015 to a high of 2.71% in June before falling back to 2.14% in March 2016. The FTSE All Share Index fell 7.3% from 3664 to 3395 and the MSCI World Index fell 5.3% from 1741 to 1648 over the 12 months to 31 March 2016.

TOTAL INVESTMENT ACTIVITY 2015/16

	Externally Managed £	Internally Managed £	Call/Notice Accounts £	Total £
Clearing Banks				
NatWest			131,970,000	131,970,000
Royal Bank of Scotland	7,000,000	1,000,000		8,000,000
Barclays Bank		7,000,000		7,000,000
Lloyds Bank		12,000,000		12,000,000
HSBC			6,000,000	6,000,000
Other Banks				
Santander			16,000,000	16,000,000
Svenska Handelsbanken			4,000,000	4,000,000
Close Brothers	1,000,000			1,000,000
Building Societies				
Nationwide		8,000,000		8,000,000
Skipton	4,000,000			4,000,000
Leeds		2,000,000		2,000,000
Principality	1,000,000	2,000,000		3,000,000
West Bromwich	4,000,000			4,000,000
Total Investments	17,000,000	32,000,000	157,970,000	206,970,000

PRUDENTIAL AND TREASURY INDICATORS 2015/16

Indicator	Description	Revised Indicator	Actual
<u>Aff.1</u>	Affordability Measure: Financing Costs as a percentage of net revenue stream		
	Overall Position	5%	5%
1a	General Fund	-8%	-7%
1b	Housing Revenue Account	15%	15%
<u>Aff.2</u>	Affordability Measure: Incremental impact of capital investment on Council Tax and Housing Rents		
2a	Council Tax increases, borrowing costs only	£0.34	£0.00
2b	Housing Rent increases, borrowing costs only	-£0.06	£0.00
<u>Aff.3</u>	Affordability Measure: Capital Expenditure (£'000s)		
	General Fund	£20,911	£17,260
	Housing Revenue Account	£10,353	£7,306
	Total Capital Expenditure	£31,264	£24,566
<u>Aff.4</u>	Affordability Measure: External Debt Level (£'000s)		
	Authorised limit, comprising	£67,000	£44,819
	- borrowing	£61,000	£43,200
	- other long term liabilities	£6,000	£1,619
	Operational boundary, comprising	£51,000	£44,819
	- borrowing	£47,000	£43,200
	- other long term liabilities	£4,000	£1,619
<u>Aff.5</u>	Affordability Measure: Capital Financing Requirement (CFR) (£'000s)		
	General Fund CFR closing balance in the year	£55,571	£61,894
	HRA CFR closing balance in the year	£2,872	£8,943
		£52,879	£52,951
<u>Pru.1</u>	Prudence Measure: Gross Debt and Capital Financing Requirement (CFR) (£'000s)		
	Gross Debt	£43,082	£44,819
	CFR (for last, current and next 2 years)	£233,184	£239,884
	Has measure been achieved?	Achieved	Achieved
	Memorandum Item : Prudence margin	£190,102	£195,065
<u>Pru.2</u>	Prudence Measure: Adoption of the CIPFA Treasury Management Code of Practice		
	Has the Code been adopted in its entirety?	Yes	Yes
<u>Pru.3</u>	Prudence Measure: Upper Limits to fixed and variable interest rate exposure		
	Upper limit to variable interest rate exposures	25%	12%
	Upper limit to fixed interest rate exposures	100%	100%
<u>Pru.4</u>	Prudence Measure: Maturity structure of borrowing		
	Loans maturing within 1 year	Upper Limit	£40m long term loans from PWLB and £3m temporary borrowing
	Loans maturing within 1 - 2 years	25%	
	Loans maturing within 2 - 5 years	25%	
	Loans maturing within 5 - 10 years	25%	
	Loans maturing in over 10 years	50%	
		100%	
<u>Pru.5</u>	Prudence Measure: Total Principal sums invested for periods of more than 364 days (£'000s)		
	Upper Investment Limit for the year	£22,000	£3,000