FAREHAM
BOROUGH COUNCIL

Report to the Executive for Decision
06 November 2017

Portfolio:	Policy and Resources
Subject:	**Treasury Management Monitoring Report 2017-18**
Report of:	Director of Finance and Resources
Strategy/Policy:	Finance Strategy
Corporate Objective:	A dynamic, prudent and progressive Council

Purpose:
This report summarises the Council's investment activity up to 30 September 2017 and provides details of the Council's money market transactions.

Under the Code of Conduct that governs the operation of the money markets, it is not possible to make public details of specific transactions. For this reason, Appendix B is included in the confidential part of the agenda.

Executive summary:
This report gives the Executive the opportunity to review the treasury management activity up to 30 September 2017 along with the Treasury and Prudential Indicators. During the first half of the year the Council operated within the Treasury and Prudential Indicators.

Council borrowing at 30 September was £42.3m and the overall investment position is set out in the following table:

Investments	Externally Managed £m	Internally Managed £m	Call Accounts £m	Money Market Funds £m	Total £m
At 1 April 2017	**3.0**	**6.0**	**0.0**	**6.0**	**15.0**
New	0	10.0	10.4	32.0	52.4
Repaid	3.0	9.0	8.4	35.8	56.2
At 30 Sept 2017	**0.0**	**7.0**	**2.0**	**2.2**	**11.2**

This compares to the same time last year where total borrowing was £42m and the total investments were £31m.

From January 2018, the council will need to maintain investments of £10million to retain its current MiFID 'professional' status and have access to the same broad range of investment products.

Recommendation:
It is recommended that the Executive notes the Treasury Management Monitoring Report for 2017/18.

Reason:
To inform the Executive of the Council's investment, borrowing and repayment activity up to 30 September 2017.

Cost of proposals:
Not applicable.

Appendices:
A: Economic Commentary and Outlook by Arlingclose
B: Investment Activity (Confidential Appendix)
C: Treasury and Prudential Indicators

Background papers: None

Reference papers:
6 February 2017 Executive Report - Treasury Management Strategy and Prudential Indicators 2017/18

FAREHAM
BOROUGH COUNCIL

Executive Briefing Paper

Date:	06 November 2017
Subject:	Treasury Management Monitoring Report 2017-18
Briefing by:	Director of Finance and Resources
Portfolio:	Policy and Resources

INTRODUCTION

1. The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management recommends that members be updated on treasury management at least twice yearly (mid-year and at year end). This report therefore ensures the Council is implementing best practice in accordance with the Code.

2. The Council's Treasury Management Strategy for 2017/18 was approved by Full Council on 24 February 2017.

3. The Council has borrowed and 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 report covers treasury activity and the associated monitoring and control of risk.

4. An economic commentary by the Council's Treasury Advisors, Arlingclose, can be found in Appendix A.

BORROWING ACTIVITY

5. At 30 September 2017, the Council held £42.3 million of loans, (an increase of £0.5 million on 31 March 2017).

6. The Council expects to borrow externally up to £10 million more in 2017/18 to part fund the capital programme.

7. The Council's main objective when borrowing continues to be striking an appropriately low risk balance between securing low interest rates and achieving cost certainty over the period for which the funds are required.

8. Affordability and the 'cost of carry' remained 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 for a significant period, lower than long-term interest rates, the Council determines it is more cost effective in the short term to use internal resources (internal borrowing) and short-term loans instead.

9. 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.

10. Borrowing activity to 30 September 2017 was:

	Balance on 31 March 2017 £'000	**Balance on 30 Sept 2017 £'000**	**Average Rate**
Long Term Borrowing	40,000	40,000	3.50%
Portchester Crematorium	1,541	2,017	0.25%
Charity of Winifred Nellie Cocks	287	288	0.50%
Total Borrowing	**41,828**	**42,305**	

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

11. The Council holds large invested funds, representing income received in advance of expenditure plus balances and reserves held.

12. The 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.

13. 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 2017/18.

14. Details on investment activity to 30 September 2017 are in Appendix B and summarised in the table below:

Investments	**Externally Managed £m**	**Internally Managed £m**	**Call Accounts £m**	**Money Market Funds £m**	**Total £m**
At 1 April 2017	**3.0**	**6.0**	**0.0**	**6.0**	**15.0**
New	0	10.0	10.4	32.0	52.4
Repaid	3.0	9.0	8.4	35.8	56.2
At 30 Sept 2017	**0.0**	**7.0**	**2.0**	**2.2**	**11.2**

15. The £3.8 million decrease in investments during the first half of the year was mainly due to the timing of precept payments, receipts of grants and progress on the Capital Programme.

REGULATORY UPDATES

Markets in Financial Instruments Directive (MiFID II)

16. Local authorities are currently treated by regulated financial services firms as professional clients who can “opt down” to be treated as retail clients instead. But from 3rd January 2018, as a result of the second Markets in Financial Instruments Directive (MiFID II), local authorities will be treated as retail clients who can “opt up” to be professional clients, providing that they meet certain criteria. (Regulated financial services firms include banks, brokers, advisers, fund managers and custodians, but only where they are selling, arranging, advising or managing designated investments).

17. In order to opt up to be a professional client, the authority must have an investment balance of at least £10 million and the person authorised to make investment decisions on behalf of the authority must have at least one year’s relevant professional experience. In addition, the firm must assess that that person has the expertise, experience and knowledge to make investment decisions and understand the risks involved.

18. If the Council were to change their status to retail client it is likely it will face increased costs and potentially restricted access to certain products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice.

19. The Council currently meets the conditions to opt up to professional status and intends to do so in the future in order to maintain their current MiFID status and to continue to have access to a broad range of investment products.

CIPFA Consultation on Prudential and Treasury Management Codes

20. In February 2017, CIPFA canvassed views on the relevance, adoption and practical application of the Treasury Management and Prudential Codes and after reviewing responses launched a further consultation on changes to the codes in August with a deadline for responses of 30th September 2017.

21. The proposed changes to the Prudential Code include the production of a new high-level Capital Strategy report to Full Council which will cover the basics of the capital programme and treasury management. The prudential indicators for capital expenditure and the authorised borrowing limit would be included in this report but other indicators may be delegated to another committee. There are plans to drop certain prudential indicators; however, local indicators are recommended for ring fenced funds (including the HRA) and for group accounts. Other proposed changes include applying the principles of the Code to subsidiaries.

22. Proposed changes to the Treasury Management Code include the potential for non-treasury investments such as commercial investments in properties in the definition of “investments” as well as loans made or shares brought for service purposes. Another proposed change is the inclusion of financial guarantees as instruments requiring risk management and addressed within the Treasury Management Strategy. Approval of the technical detail of the Treasury Management Strategy may be delegated to a committee rather than needing approval of Full Council. There are also plans to drop or alter some of the current treasury management indicators.

23. CIPFA intends to publish the two revised Codes towards the end of 2017 for implementation in 2018/19, although CIPFA plans to put transitional arrangements in place for reports that are required to be approved before the start of the 2018/19 financial year.

24. The Department of Communities and Local Government (DCLG) and CIPFA wish to have a more rigorous framework in place for the treatment of commercial investments as soon as is practical. It is understood that DCLG will be revising its Investment Guidance (and its MRP guidance) for local authorities in England; however there have been no discussions with the devolved administrations yet.

BUDGETED INCOME AND OUTTURN

25. The UK Bank Rate had been maintained at 0.5% since March 2009 until August 2016, when it was cut to 0.25%. The Bank of England's Monetary Policy Committee has changed its rhetoric, implying a rise in Bank Rate in "the coming months". Arlingclose is not convinced the UK's economic outlook justifies such a move at this stage, but the Bank's interpretation of the data seems to have shifted.

26. This decision is still very data dependant and Arlingclose is, for now, maintaining its central case for a Bank Rate at 0.25% for the foreseeable future.

27. The Council's budgeted investment income for the year is estimated at £499,900. As all the Council's surplus cash continues to be invested in short-dated money market instruments, it will most likely result in a fall in investment income over the year.

COMPLIANCE WITH TREASURY AND PRUDENTIAL INDICATORS

28. The Council confirms compliance with its Treasury and Prudential Indicators for 2017/18, which was set on 24 February 2017 as part of the Council's Treasury Management Strategy Statement.

29. Performance for the first half of the year is shown in Appendix C. During the financial year to date the Council has operated within the treasury limits and prudential indicators.

RISK ASSESSMENT

30. In the current economic climate, there are risks that financial institutions holding Council investments could default and be unable to fulfil their commitments to repay the sums invested with them.

31. To help mitigate this risk, the Council maintains a list of approved institutions based on a grading system operated by the Council's treasury management advisors. Maximum limits are also set for investments with individual institutions.

Enquiries:

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