FAREHAM
BOROUGH COUNCIL

Report to the Executive for Decision
2 September 2013

Portfolio:	Policy and Resources
Subject:	**Treasury Management Monitoring Report 2013/14**
Report of:	Director of Finance and Resources
Strategy/Policy:	Finance and Treasury Management Strategies
Corporate Objective:	A dynamic, prudent and progressive council

Purpose:
This report summarises the Council's investment activity up to 30 June 2013 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 A 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 June 2013 along with the Treasury and Prudential Indicators.

The overall position is set out in the following table:

Investments	Externally Managed £m	Internally Managed £m	Call Accounts £m	Total £m
At 1 April 2013	**10.0**	**12.0**	**10.8**	**32.8**
New	4.0	4.0	37.4	45.4
Repaid	4.0	4.0	28.6	36.6
At 30 June 2013	**10.0**	**12.0**	**19.6**	**41.6**

The actual fixed term investments are set out in Appendix A with more detailed information set out in the briefing paper.

Performance for the first quarter of the year for the Treasury and Prudential Indicators are shown in detail in Appendix B. During the financial year to date the Council has operated within the treasury limits and Prudential Indicators.

Recommendation:
That the treasury management monitoring report be noted.

Reason: To inform the Executive of the Council's investment, borrowing and repayment activity up to 30 June 2013.

Cost of proposals: Not applicable.

Appendices	**A:**	Externally & Internally Managed Investments (Confidential Appendix)
	B:	Q1 Treasury and Prudential Indicators
	C:	Treasury and Prudential Indicators Explained

Background papers:
Exempt by virtue of Paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972.

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Executive Briefing Paper

Date: 2 September 2013

Subject: Treasury Management Monitoring Report 2013/14

Briefing by: Director of Finance and Resources

Portfolio: Policy and Resources

INTRODUCTION

1. The Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice for Treasury Management recommends that members should be updated on treasury management activities at least twice a year, but preferably quarterly. This report therefore ensures this Council is implementing best practice in accordance with the Code.

2. The total amount of fixed term investments and call accounts as at 30 June 2013 was £41.6 million, as summarised below. The movements during the year for fixed term investments are detailed in Appendix A.

Investments	Externally Managed £m	Internally Managed £m	Call Accounts £m	Total £m
At 1 April 2013	**10.0**	**12.0**	**10.8**	**32.8**
New	4.0	4.0	37.4	45.4
Repaid	4.0	4.0	28.6	36.6
At 30 June 2013	**10.0**	**12.0**	**19.6**	**41.6**

3. The increase in funds of £8.8 million during the first quarter was mainly due to the timing of precept payments, receipts of grants and progress on the Capital Programme.

INVESTMENT STRUCTURE

4. The structure of the investments at 30 June is shown in the table below. Over the past few years, most investments have been held on short periods to mitigate the risks that have been seen during the recession. At the same time, officers have actively sought to spread investments across a wider range of counterparties rather than operating at the upper limit for investments to limit the exposure to financial loss.

5. Throughout this period of uncertainty, officers have been taking advice from the Council's retained treasury advisers, Sector, to ensure that decisions are taken in light of the latest facts at the time. This has given rise to lower interest rates

being secured but this is the lowest priority consideration compared to the security of investments and the liquidity of cash flow.

6. The Council's fixed term investments are partly managed externally by Tradition UK Ltd. The role of the broker is to determine the most appropriate investment option within criteria set by the Council. All cash transfers are made by Council officers and Executive approval has been given for the allocation of up to £13 million to the externally managed portfolio. This retains sufficient funds within the direct management of officers, while still ensuring that maximum yield is achieved from the longer term investments.

7. The investment structure is sufficient to meet the capital programme and other large cash outflows.

Investment Structure	**External £m**	**Internal £m**	**Call £m**	**Total £m**
For periods of less than 1 month	1.0	0	15.6	16.6
For periods of 1 to 3 months	2.0	3.0	0	5.0
For periods of 3 to 6 months	3.0	0	4.0	7.0
For periods of 6 to 12 months	4.0	9.0	0	13.0
For periods of 1 to 2 years	0	0	0	0
Total Investments at 30 June 2013				
Investments for periods < 365 days	10.0	12.0	19.6	41.6
Investments for periods 365+ days	0	0	0	0

8. To increase the liquidity of the Council's investments, call accounts with Nat West (including a 95 day notice account), Santander and HSBC are being used. These accounts offer quick access to funds however they do attract a lower rate of interest than some of the fixed term investments shown in the table above.

9. The balance within each call account as at 30 June 2013 is set out in the following table:-

Call Accounts	**£m**
NatWest	7.6
NatWest - 95 day notice	4.0
Santander UK	2.0
HSBC	6.0
Total	**19.6**

ECONOMIC OUTLOOK

10. Summary for the UK:

- Mark Carney started on 1st July as the new Governor of the Bank of England. His appointment could lead to some changes to the way the MPC operates and makes decisions and announcements.
- Growth in Q1 of 2013 was confirmed at +0.3%. Q2 looks likely to be even higher at around +0.5%. The so called double dip recession at the beginning of 2012 was erased by the latest revision of statistics.
- Business surveys, consumer confidence, consumer borrowing and house prices are all on the up and may help to create a wide spread feel good

factor. But this is still a long way away from the UK getting back to strong growth.
- In February 2013 Moody's downgraded the UK's AAA credit rating one notch to AA+ and Fitch followed suit in April. There was little reaction in financial markets, as this had been widely anticipated.

11. Economic forecasting remains difficult with so many external influences weighing on the UK. Major volatility in bond yields is likely during 2013/14 as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, and safer bonds. Key areas of uncertainty include:

- The potential for a significant increase in negative reactions of populaces in Eurozone countries against austerity programmes, especially in countries with very high unemployment rates e.g. Greece and Spain, which face huge challenges in engineering economic growth to correct their budget deficits on a sustainable basis.
- The Italian political situation is frail and unstable.
- Problems in other Eurozone heavily indebted countries could also generate safe haven flows into UK gilts.
- Monetary policy action failing to stimulate growth in western economies, especially the Eurozone and Japan.
- The potential for weak growth or recession in the UK's main trading partners - the EU and US.
- The impact of the UK Government's austerity plan in dampening confidence and growth.
- Geopolitical risks e.g. Syria, Iran, North Korea.

12. Given the generally weak outlook for economic growth, Sector sees the prospects for any increase in Bank Rate before 2015 as limited. Indeed, the first increase could be even further delayed if the tentative signs of growth failed to be maintained.

INTEREST RATES

13. The base rate has remained at 0.5% since March 2009. The Sector central forecast is for the first increase in Bank Rate to be in the first quarter of 2015.

14. Investment rates available in the market have continued at historically low levels and have fallen further during the quarter as a result of the Bank of England's Funding for Lending Scheme. Investment income has dropped significantly over the past few years as long term investments with high interest rates have matured. Actual investment income for 2012/13 was £647,800 with the budget for 2013/14 set at £737,700 for the General Fund and HRA.

BORROWING

15. The Council's external long term debt amounted to £40.6 million as at 1 April 2013. This is as a result of the HRA reforms (£40m) and the Hampshire County Council interest free loan for Portchester Community Centre (£0.6m). Further borrowing is anticipated in 2013/14 in relation to the Solent Growing Places Fund for Daedalus.

16. The Council has taken out ten £4 million loans from the PWLB with duration of between 40 and 50 years at an average interest rate of 3.50% as detailed in the table below:-

Repayment Date	Loan Amount	Interest Rate
30/09/2052	£4m	3.52%
30/09/2053	£4m	3.51%
30/09/2054	£4m	3.51%
30/09/2055	£4m	3.51%
30/09/2056	£4m	3.50%
30/09/2057	£4m	3.50%
30/09/2058	£4m	3.50%
30/09/2059	£4m	3.49%
30/09/2060	£4m	3.49%
30/09/2061	£4m	3.48%
Total	**£40m**	**3.50% average**

17. Interest payable for 2013/14 is budgeted at £1,870,900 and will be met by the HRA. £1,400,400 relates to the PWLB loans and £470,500 for interest on internal borrowing between the General Fund and the HRA.

STRATEGY COMPLIANCE

18. The Council's Treasury Management Strategy Statement for 2013/14, which includes the Annual Investment Strategy 2013/14, was approved by the Council on 22 February 2013. It sets out the Council's investment priorities as being:

- Security of capital;
- Liquidity; and
- Yield

19. The Council will also aim to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term to cover cash flow needs but also to seek out value available in higher rates in periods up to 12 months with highly credit rated financial institutions.

20. The compliance with the various elements of the strategy are set out in the following table:-

Compliance on Individual Elements	**Yes/No**	**Notes**
Borrowing only up to “supported” level	Yes	No borrowing this quarter
All investments with approved institutions	Yes	Treasury management advisors provide updated list of approved institutions weekly
All individual investments within prescribed financial limits	Yes	There is currently 1 institution where the total investment is at the maximum level. This is for Lloyds TSB Bank where the limit is £8m

21. No changes to the Council’s Treasury Management Strategy Statement and Annual Investment Strategy 2013/14 are considered necessary at this time as the rules currently being applied to investments are much tighter than those approved within the Treasury Management Strategy.

COMPLIANCE WITH TREASURY AND PRUDENTIAL LIMITS

22. It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators (affordable limits) were approved by the Executive at its meeting on 11 February 2013.

23. Performance for the first quarter of the year is shown in Appendix B and the purpose of each indicator is explained in more detailed in Appendix C. During the financial year to date the Council has operated within the treasury and prudential indicators.

RISK ASSESSMENT

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

Reference Papers:
11 February 2013 Executive Report - Treasury Management Strategy and Prudential Indicators 2013/14

Appendix B

2012/13 Prudential and Treasury Indicators - Quarter 1 Performance

Indicator	Description	Approved Indicators 2013/14	Quarter 1 Position	Performance Rating
Aff.1 1a 1b	**Affordability Measure: Financing Costs as a percentage of net revenue streams** Overall Position General Fund Housing Revenue Account	 2% -14% 15%	 2.2% -3.6% 16.3% (estimated)	☺
Aff.2 2a 2b	**Affordability Measure: Incremental impact of capital investment on Council Tax and Housing Rents** Council Tax increases, borrowing costs only Housing Rent increases, borrowing costs only	£1.15 £0.65	No unsupported borrowing undertaken, therefore no affect on rent or council tax increases	☺
Aff.3	**Affordability Measure: Capital Expenditure (£'000s)** General Fund Housing Revenue Account Total Capital Expenditure	**Estimate to 30 Jun 13** £565 <u>£502</u> £1,067	**Actual to 30 Jun 13** £503 <u>£456</u> £959	☺
Aff.4	**Affordability Measure: External Debt Level (£'000s)** Authorised limit, comprising *- borrowing* *- other long term liabilities* Operational boundary, comprising *- borrowing* *- other long term liabilities*	 £61,000 *£57,000* *£4,000* £49,000 *£47,000* *£2,000*	Long term external debt is £40.6m and short term debt is £1.429m	☺
Aff.5	**Affordability Measure: Capital Financing Requirement (£'000s)** General Fund CFR closing balance in the year HRA CFR closing balance in the year	£51,051 -£2,754 £53,805	No anticipated change to the planned position for CFR items	☺

Indicator	Description	Approved Indicators 2013/14	Quarter 1 Position	Performance Rating
Pru.1	**Prudence Measure: Gross Debt and Capital Financing Requirement (CFR), (£'000s)** Gross External Borrowing level CFR (for last, current and next 2 years) Has measure been achieved? Memorandum Item: Prudence margin	 -£42,271 £204,204 Achieved £161,933	 -£42,029 £204,204 Achieved £162,175	☺
Pru.2	**Prudence Measure: Adoption of the CIPFA Treasury Management Code of Practice** Has the Code been adopted in its entirety?	Yes	Yes	☺
Pru.3	**Prudence Measure: Upper Limits to fixed and variable interest rate exposure** Upper limit to variable interest rate exposures Upper limit to fixed interest rate exposures	25% 100%	All investments at fixed rates.	☺
Pru.4	**Prudence Measure: Maturity structure of borrowing** Loans maturing within 1 year Loans maturing within 1 - 2 years Loans maturing within 2 - 5 years Loans maturing within 5 - 10 years Loans maturing in over 10 years	Upper Limit 25% 25% 25% 50% 100%	No borrowing undertaken in Quarter 1	☺
Pru.5	**Prudence Measure: Total Principal sums invested for periods of more than 364 days (£'000s)** Upper Investment Limit for the year	£16,000,000	£0m 1-2 years £0m 2-3 years £0m 3-4 years	☺

APPENDIX C

Details of the Treasury and Prudential Indicators

This appendix explains each of the prudential indicators, as defined in the Prudential Code for Capital Finance in Local Authorities and the Treasury Management in Public Service Code of Practice.

Affordability

Aff.1: Financing costs as a percentage of net revenue stream

This compares the total principal and net interest payments on external debt less interest and investment income to the overall total revenue spending of the authority. The indicator must be calculated separately for the General Fund and Housing Revenue Account (HRA).

Aff.2: The incremental impact of capital investment on the Council Tax and Housing Rents

This indicator requires the General Fund net revenue streams to be converted into an estimated Band D Council Tax for each of the next three years. This will mean making assumptions on the levels of Government grant and Non Domestic Rates expected as well as the Council Tax base and spending plans. Only the element of any increase/decrease in Council Tax that relates to the Council's capital investment plans is reported in the indicator. A similar indicator must be calculated for average weekly rents in the HRA.

Aff.3: Capital expenditure

This indicator reports the Council's capital expenditure for the current year.

Aff.4: External debt

This indicator reports on the external debt limits (made up of borrowing and other long term liabilities). The two limits set are:-

The *authorised limit*. This is the maximum amount the authority allows itself to borrow.

The *operational boundary*. This reflects the most likely (prudent) but not worst case scenario of the debt position of the authority. This is also an "upper" limit, so does not reflect the expected external debt level for the Council on a day to day basis, but should link directly to capital spending plans, the capital financing requirement and daily cash-flows.

There may be occasions when the operational boundary for borrowing is temporarily breached - for example, if a capital receipt is not received on the due date. Such breaches must be monitored to identify trends, but do not need to be reported. On very rare occasions, the authorised limit may be breached and this must be reported to members.

Aff.5: The Capital Financing Requirement (CFR)

This indicator reports the actual capital financing requirement (CFR) for the General Fund and HRA. The CFR comprises the sum of the value of fixed assets (land, buildings etc), deferred charges (spending on assets not owned by the Council, such as capital grants to housing associations) and other capital accounts on the balance sheet (revaluation reserve and capital adjustment account). By adding these values together, the total represents a good approximation of how much capital investment has been funded from borrowing.

Prudence

The aim of this category of indicator is to ensure that medium and long term borrowing is only for capital purposes and that authorities are not taking out long term borrowing to fund revenue spending.

Pru.1: Gross external borrowing and the capital financing requirement

This indicator is used to compare the gross external borrowing against the total capital financing requirement (see Aff.5 above) for current year plus any additions to the total capital financing requirement for the coming year and two following years. The gross external borrowing figure should always be the lower figure.

Pru.2: Adoption of the CIPFA Treasury Management Code of Practice

The Code requires an explicit statement from the Authority that it has adopted the above Code published by the Chartered Institute of Public Finance and Accountancy, in full.

Pru.3: Upper limits to fixed and variable rate exposures

This indicator sets upper limits on the amount of net borrowing (total borrowing less investments) with fixed interest rates and variable interest rates for a three year period. By applying these thresholds, the exposure to fluctuations in interest rates can be controlled.

Pru.4: Maturity structure of borrowing

This indicator sets upper and lower limits on the amount of borrowing due to be repaid in a given period on fixed rate borrowing. The purpose of this indicator is to ensure that the Council has a balanced portfolio of debt, avoiding any major peaks and troughs over the life of the total debt.

Pru.5: Total principal sums invested for periods of more than 364 days

This sets a limit on the amount of money than can be invested for more than one year.