FAREHAM
BOROUGH COUNCIL

Report to the Executive for Decision
10 February 2014

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 31 December 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 31 December 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	10.0	15.0	91.8	116.8
Repaid	10.0	7.0	84.9	101.9
At 31 Dec 2013	**10.0**	**20.0**	**17.7**	**47.7**

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 half 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 31 December 2013.

Cost of proposals:
Not applicable.

Appendices A: Externally & Internally Managed Investments (Confidential Appendix)
B: Q3 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: 10 February 2014

Subject: Treasury Management Monitoring Report 2013/14

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 activities regularly. 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 31 December 2013 was £47.7 million, as summarised below. The movements during the year for fixed term investments are detailed in Appendix A.

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New	10.0	15.0	91.8	116.8
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3. The increase in funds of £14.9 million during the first 9 months of the year 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 31 December 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 advisor, Capita Asset Services (previously known as 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	0	0	15.7	15.7
For periods of 1 to 3 months	0	5.0	0	5.0
For periods of 3 to 6 months	4.0	4.0	2.0	10.0
For periods of 6 to 12 months	4.0	11.0	0	15.0
For periods of 1 to 2 years	2.0	0	0	2.0
Total Investments at 31 Dec 2013				
Investments for periods < 365 days	8.0	20.0	17.7	45.7
Investments for periods 365+ days	2.0	0	0	2.0

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 31 December 2013 is set out in the following table:-

Call Accounts	**£m**
NatWest	2.7
NatWest - 95 day notice	7.0
Santander - 95 day notice	2.0
HSBC	6.0
Total	**17.7**

ECONOMIC UPDATE

10. Until 2013, the economic recovery in the UK since 2008 had been the worst and slowest recovery in recent history. However, growth has rebounded during 2013 to surpass all expectations, propelled by recovery in consumer spending and the housing market.

11. After strong UK growth of 0.7% in quarter 2 and 0.8% in quarter 3, it appears that the UK GDP is likely to have grown at an even faster pace in Q4 of 2013. Forward surveys are also very encouraging in terms of strong growth and there are positive indications that recovery is broadening away from reliance on consumer spending and the housing market into construction, manufacturing, business investment and exporting.

12. This strong growth has resulted in unemployment falling much faster towards the threshold of 7%, set by the MPC before it said it would consider any increases in Bank Rate, than it expected last August when that threshold was initially set. Accordingly, markets are expecting a first increase in early 2015 though recent comments from MPC members have emphasised they would want to see strong growth well established, and an increase in real incomes, before they would consider raising Bank Rate.

13. Also encouraging has been a sharp fall in inflation (CPI) to 2.1% in November and forward indications are that inflation will continue to be subdued. The return to strong growth has also helped lower forecasts for the increase in Government debt by £73bn over the next five years, as announced in the Autumn Statement, and fostered optimism for achieving a balance in the cyclically adjusted budget within five years, a year earlier than previously forecast.

14. Forward surveys are currently very positive in indicating that growth prospects are also strong for 2014, not only in the UK economy as a whole, but in all three main sectors, services, manufacturing and construction. This is very encouraging as there does need to be a significant rebalancing of the economy away from consumer spending to construction, manufacturing, business investment and exporting in order for this start to recovery to become more firmly established.

15. One drag on the economy is that wage inflation continues to remain significantly below CPI inflation so disposable income and living standards are under pressure, although income tax cuts have ameliorated this to some extent. Labour productivity must improve significantly before increases in pay rates are warranted.

16. With regard to the US, the main world economy, it faces similar debt problems to those of the UK, but thanks to reasonable growth, cuts in government expenditure and tax rises, the annual government deficit has been halved from its peak without appearing to do too much damage to growth, although labour force participation rates remain lower than ideal.

17. As for the Eurozone, concerns have subsided considerably in 2013. However, sovereign debt difficulties have not gone away and major concerns could return in respect of any countries that do not dynamically address fundamental issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy (as Ireland has done).

INTEREST RATES

18. The base rate has remained at 0.5% since March 2009. Capita Asset Services undertook a review of its interest rate forecasts in late November, after the Bank of England's latest quarterly Inflation Report. The latest forecast now includes a first increase in Bank Rate in quarter 2 of 2016 (previously quarter 3).

19. 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

20. 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).

21. 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**

22. 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

23. 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

24. 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.

25. 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 are currently 7 institutions where the total investment is at the maximum level. They are Lloyds Bank (£8m limit), Barclays Bank, HSBC, Santander and Nationwide BS (£6m limit), Skipton BS and West Brom BS (£2m limit).

26. 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

27. 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.

28. Performance up to 31 December 2013 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

29. 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