

Bath & North East Somerset Council

MEETING:	Cabinet	
MEETING DATE:	12th November 2014	
TITLE:	Treasury Management Monitoring Report to 30th September 2014	EXECUTIVE FORWARD PLAN REFERENCE: E 2652
WARD:	All	
AN OPEN PUBLIC ITEM		
List of attachments to this report: Appendix 1 – Performance Against Prudential Indicators Appendix 2 – The Council’s Investment Position at 30 th September 2014 Appendix 3 – Average monthly rate of return for 1 st 6 months of 2014/15 Appendix 4 – The Council’s External Borrowing Position at 30 th September 2014 Appendix 5 – Arlingclose’s Economic & Market Review Q2 of 2014/15 Appendix 6 – Interest & Capital Financing Budget Monitoring 2014/15 Appendix 7 – Summary Guide to Credit Ratings Appendix 8 – Proposed amendments to the 2014/15 Treasury Management Strategy		

1 THE ISSUE

1.1 In February 2012 the Council adopted the 2011 edition of the CIPFA Treasury Management in the Public Services: Code of Practice, which requires the Council to approve a Treasury Management Strategy before the start of each financial year, review performance during the year, and approve an annual report after the end of each financial year.

1.2 This report gives details of performance against the Council’s Treasury Management Strategy and Annual Investment Plan 2014/15 for the first six months of 2014/15.

2 RECOMMENDATION

The Cabinet agrees that:

2.1 the Treasury Management Report to 30th September 2014, prepared in accordance with the CIPFA Treasury Code of Practice, is noted

2.2 the Treasury Management Indicators to 30th September 2014 are noted.

2.3 this Treasury Management Report and attached appendices are reported to November Council and December Corporate Audit Committee.

2.4 The proposed amendments to the 2014/15 Treasury Management Strategy set out in paragraphs 5.19-23 and Appendix 8 are reported to November Council for approval.

3 RESOURCE IMPLICATIONS

3.1 The financial implications are contained within the body of the report.

4 STATUTORY CONSIDERATIONS AND BASIS FOR PROPOSAL

4.1 This report is for information only.

5 THE REPORT

Summary

5.1 The average rate of investment return for the first six months of 2014/15 is 0.43%, which is 0.04% above the benchmark rate.

5.2 The Council's Prudential Indicators for 2014/15 were agreed by Council in February 2014 and performance against the key indicators is shown in **Appendix 1**. All indicators are within target levels, with the exception of one voluntary indicator, measuring the liquidity of the council's investments, as detailed in 5.13 and Appendix 1(8).

Summary of Returns

5.3 The Council's investment position as at 30th September 2014 is given in **Appendix 2**. The balance of deposits as at 30th June 2014 and 30th September 2014 are also set out in the pie charts in this appendix.

5.4 The Council is the accountable body for the West of England Revolving Investment Fund (RIF) and received grant funding of £57 million at the end of the 2011/12 financial year. The Council acts as an agent and holds these funds on behalf of the West of England Local Enterprise Partnership until they are allocated in the form of repayable grants to the constituent Local Authorities to meet approved infrastructure costs. Since these funds are invested separately from the Council's cash balances and have been placed short term with the Debt Management Office and other Local Authorities, they are excluded from all figures given in this report. The current value of the fund is £44.8 million.

5.5 Gross interest earned on investments for the first six months totalled £81k. Net interest, after deduction of amounts due to Schools, the West of England Growth Points, CHC and other internal balances, is £43k. **Appendix 3** details the investment performance, showing the average rate of interest earned over this period was 0.43%, which was 0.04% above the benchmark rate of average 7 day LIBID +0.05% (0.39%).

Summary of Borrowings

5.6 No new borrowing has taken place in the first half of 2014/15. The Council's total borrowing was £70 million as at the 30th September 2014. The Council's Capital Financing Requirement (CFR) as at 31st March 2014 was £153 million with a projected total of £215 million by the end of 2014/15 based on the capital programme approved at February 2014 Council. This represents the Council's

underlying need to borrow to finance capital expenditure, and demonstrates that the borrowing taken to date relates to funding historical capital spend.

5.7 Subsequent to the end of the reporting period, £8 million of borrowing was arranged on 2nd October with two Local authorities for a two year period. The borrowing was undertaken to replenish cash-flow used to fund a specific commercial estate investment opportunity.

5.8 Following Local Government Reorganisation in 1996, Avon County Council's residual debt is administered by Bristol City Council. All successor Unitary Authorities make an annual contribution to principal and interest repayment, for which there is a provision in the Council's revenue budget. The amount of residual debt outstanding as at 31st March 2014 apportioned to Bath & North East Somerset Council is £14.54m. Since this borrowing is managed by Bristol City Council and treated in the Council's Statement of Accounts as a deferred liability, it is not included in the borrowing figures referred to in paragraph 5.6.

5.9 The borrowing portfolio as at 30th September 2014 is shown in **Appendix 4**.

Strategic & Tactical Decisions

5.10 As shown in the charts at **Appendix 2**, investments continue to be focussed on UK banks and building societies that have either already or are likely to receive support from the UK Government should they experience financial difficulties. To increase diversification, the Council invests in AAA rated Money Market funds, with a balance of £3.7m invested in these as at 30th September 2014.

5.11 The Council continues to not hold any direct investments with banks in countries within the Eurozone reflecting both on the underlying debt issues in some Eurozone countries and the low levels of interest rates. The Council's investment counterparty list does not currently include any banks from Portugal, Ireland, Greece, Spain and Italy.

5.12 The Council's average investment return is running slightly above the budgeted level of 0.35%.

5.13 The Council has adopted a voluntary indicator of its exposure to liquidity risk, which is that the amount of cash available from maturing investments, to meet unexpected payments within a rolling three month period without additional borrowing, should not fall below £15m. The liquidity balance figure on 30th September 2014 was below the indicator (£9.85m). This was due to delaying the planned borrowing by a week in order to take advantage of short term inter-authority rates dropping at the beginning of each month. This borrowing of £8m was arranged on 2nd October at a lower cost than the market was offering during the previous weeks.

Future Strategic & Tactical Issues

5.14 Our treasury management advisors economic and market review for the second quarter 2014/15 is included in **Appendix 5**.

5.15 The Bank of England base rate has remained constant at 0.50% since March 2009. The stronger economic growth seen in the UK over the past six months is likely to use up spare capacity more quickly than previously assumed and the

Council's treasury advisors, Arlingclose, have brought forward their estimate of the timing for the first rise in Bank Rate to Q3 2015.

5.16 In their opinion, in addition to two MPC members having voted for a rate rise in August and September, the rhetoric from MPC members has certainly become more hawkish, but the lack of inflationary signals is expected to allow policymakers to hold off monetary tightening for longer than the market currently expects. However, the near-term risk is that the Bank Rate could rise sooner than anticipated.

5.17 The benefits of the Council's current policy of internal borrowing are monitored regularly against the likelihood that long term borrowing rates are forecast to rise in future years. The focus is now on the rate of increase and the medium-term peak and, in this respect, the current forecast is that rates will rise slowly and to a lower level than in the past.

5.18 Future borrowing is therefore likely to be driven by a need to maintain an appropriate working cash balance rather than any immediate changes to interest rates.

5.19 The UK is implementing the final bail-in provisions of the EU Bank Recovery and Resolution Directive to commence in January 2015, a year ahead of most other countries. Credit rating agencies have stated they plan to review EU banks' ratings in line with each country's implementation of the directive. Many UK banks have standalone ratings in the "BBB" category, with uplifts for potential government support taking them into the "A" category. Arlingclose advise there is therefore a realistic risk that some major UK banks' credit ratings will fall below A- this financial year if this uplift is removed.

5.20 The Council has two broad options to respond to this risk:

a) amend the Treasury Management Strategy to allow investment in lower rated UK banks, or

b) prepare to invest without using any of the major UK banks.

5.21 Although it may be possible to operate without these banks, by investing more money in Money Market Funds, for example, Arlingclose have stated that they may continue to advise on investments in the major UK banks if they become rated BBB+.

5.22 It is therefore recommended that the Council is asked to respond by preparing to amend the 2014/15 Treasury Management Strategy in line with the changes shown at **Appendix 8** in order to be able to respond to the changes that may occur in January 2015.

5.23 The s.151 Officer will consider the investment advice provided by Arlingclose at the time of any ratings change, should it occur, before any investments are made with potentially affected UK counterparties.

Budget Implications

5.24 A breakdown of the revenue budget for interest and capital financing and the forecast year end position based on the period April to September is included in **Appendix 6**. This is currently forecast to remain on target for 2014/15.

5.25 This position will be kept under review during the remainder of the year, taking into account the Council's cash-flow position and the timing of any new borrowing required.

6 RATIONALE

6.1 The Prudential Code and CIPFA's Code of Practice on Treasury Management requires regular monitoring and reporting of Treasury Management activities.

7 OTHER OPTIONS CONSIDERED

7.1 None.

8 CONSULTATION

8.1 Consultation has been carried out with the Cabinet Member for Community Resources, Section 151 Finance Officer, Chief Executive and Monitoring Officer.

8.2 Consultation was carried out via e-mail.

9 RISK MANAGEMENT

9.1 The Council's lending & borrowing list is regularly reviewed during the financial year and credit ratings are monitored throughout the year. All lending/borrowing transactions are within approved limits and with approved institutions. Investment and Borrowing advice is provided by our Treasury Management consultants Arlingclose.

9.2 The CIPFA Treasury Management in the Public Services: Code of Practice requires the Council nominate a committee to be responsible for ensuring effective scrutiny of the Treasury Management Strategy and policies. The Corporate Audit Committee carries out this scrutiny.

9.3 In addition, the Council maintain a risk register for Treasury Management activities, which is regularly reviewed and updated where applicable during the year.

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Background papers	<i>2014/15 Treasury Management & Investment Strategy 1st Quarter Treasury Performance Report (Cabinet)</i>
Please contact the report author if you need to access this report in an alternative format	