ITEM NO	

REPORT TO EXECUTIVE

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DATE	**3 July 2018**
PORTFOLIO	**Executive**
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Annual Treasury Management Report
Review of 2017/18 Activity

PURPOSE

1. To inform members of the Council's treasury management activity during 2017/18.

RECOMMENDATION

2. That the Executive recommends that Full Council note the annual treasury management activity for the year ended 31 March 2018.

REASONS FOR RECOMMENDATION

3 To comply with the regulations issued under the Local Government Act 2003 to produce an annual treasury management report review of activities and the actual prudential and treasury indicators for 2017/18. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code). Performance against the approved prudential and treasury indicators are shown in Appendix 1.

During 2017/18 the minimum reporting requirements were that Full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 22 February 2017)
- a mid-year treasury update report (Council 22 November 2017)
- an annual review following the end of the year describing the activity compared to the strategy (this report).

The regulatory environment places responsibility on Members for the review and scrutiny of treasury management policy and activities. This report is therefore important, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by Members.

This Council confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Scrutiny Committee before they were reported to Full Council. Member training on treasury management issues was undertaken during the year on 7 November 2017 in order to support Members' scrutiny role.

SUMMARY OF KEY POINTS

4. **The Economy and Interest Rates**

During the calendar year of 2017, there was a major shift in expectations in financial markets in terms of how soon the Bank Rate would start on a rising trend. After the UK economy surprised on the upside with strong growth in the second half of 2016, growth in 2017 was disappointingly weak in the first half of the year which meant that growth was the slowest for the first half of any year since 2012. The main reason for this was the sharp increase in inflation caused by the devaluation of sterling after the EU referendum, feeding increases into the cost of imports into the economy. This caused a reduction in consumer disposable income and spending power as inflation exceeded average wage increases. Consequently, the services sector of the economy, accounting for around 75% of GDP, saw weak growth as consumers responded by cutting back on their expenditure. However, growth did pick up modestly in the second half of 2017.

Consequently, market expectations during the autumn rose significantly that the Monetary Policy Committee (MPC) would be heading in the direction of imminently raising the Bank Rate. The minutes of the MPC meeting of 14 September indicated that the MPC was likely to raise the Bank Rate very soon. The 2 November MPC quarterly Inflation Report meeting duly delivered by raising the Bank Rate from 0.25% to 0.50%. The 8 February 2018 MPC meeting minutes then revealed another sharp hardening in MPC warnings on a more imminent and faster pace of increases in the Bank Rate than had previously been expected. Market expectations for increases in the Bank Rate, therefore, shifted considerably during the second half of 2017/18 and resulted in investment rates from 3 to 12 months increasing sharply during the spring quarter.

PWLB borrowing rates increased correspondingly to the above developments with the shorter term rates increasing more sharply than longer term rates. In addition, UK gilts have moved in a relatively narrow band this year, within 0.25% for much of the year, compared to US treasuries. During the second half of the year, there was a noticeable trend in treasury yields being on a rising trend with the Fed raising rates by 0.25% in June, December and March, making six increases in all from the floor. The effect of these three increases was greater in shorter term rather than longer term yields.

The major UK landmark event of the year was the inconclusive result in the general election on 8 June. However, this had relatively little impact on financial markets.

5. **The Strategy for 2017/18**

The expectation for interest rates within the treasury management strategy for 2017/18 anticipated that the Bank Rate would not start rising from 0.25% until quarter 2 2019 and then only increase once more before 31 March 2020. There would also be gradual rises in medium and longer term fixed borrowing rates during 2017/18 and the two subsequent financial years. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

In this scenario, the treasury strategy was to postpone borrowing to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

During 2017/18, longer term PWLB rates were volatile but with little overall direction, whereas shorter term PWLB rates were on a rising trend during the second half of the year.

6. **The Borrowing Requirement and Debt**

The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR). The table below shows the Council's CFR for 2017/18.

£m	31 March 2017 Actual	31 March 2018 Budget	31 March 2018 Actual
CFR General Fund	28.6	31.8	30.2

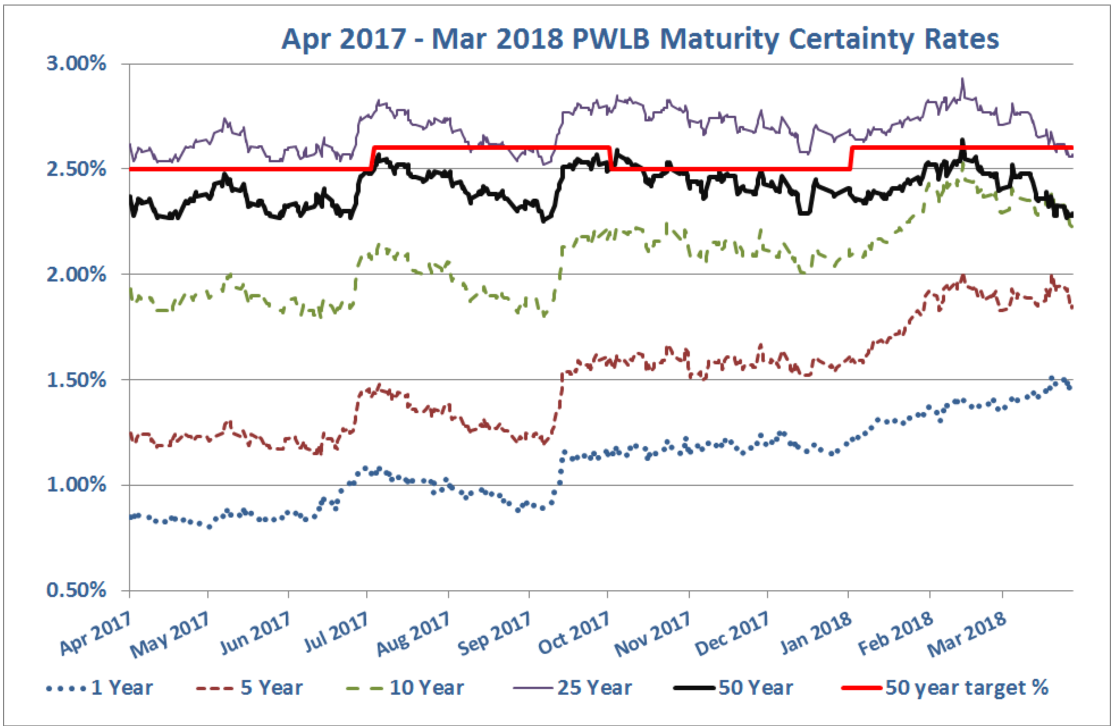
7. **Borrowing Rates in 2017/18**

PWLB certainty maturity borrowing rate

As depicted in the graph below, PWLB 25 and 50 year rates have been volatile during the year with little consistent trend. However, shorter rates were on a rising trend during the second half of the year and reached peaks in February / March.

During the year, the 50 year PWLB target (certainty) rate for new long term borrowing was 2.50% in quarters 1 and 3 and 2.60% in quarters 2 and 4.

The graph for PWLB rates show, for a selection of maturity periods, the average borrowing rates, the high and low points in rates, spreads and individual rates at the start and the end of the financial year.



8. **<u>Borrowing Outturn for 2017/18</u>**

Borrowing – the following PWLB loans were taken during the year:

Date	Lender	Principal	Type	Interest Rate	Maturity
31/8/17	PWLB	£1.5m	Maturity	2.32%	42.5 years
09/10/17	PWLB	£1m	Maturity	2.57%	41.5 years
30/10/17	PWLB	£1m	Maturity	2.58%	40.5 years
19/12/17	PWLB	£1m	Maturity	2.37%	39 years

This compares with a budget assumption of borrowing at an interest rate of 3%

Rescheduling – No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Repayments – The following PWLB loans were repaid during the year, as scheduled:

Date	Lender	Principal	Balance at Repayment	Type	Interest Rate	Duration
31/3/18	PWLB	£1m	£1m	Maturity	4.55%	12 years

9. **<u>Investment Rates in 2017/18</u>**

Investments rates for 3 months and longer have been on a rising trend during the second half of the year in the expectation of the Bank Rate increasing from its floor of 0.25%, and reached a peak at the end of March. The Bank Rate was duly raised from 0.25% to 0.50% on 2 November 2017 and remained at that level for the rest of the year. However, further increases are expected over the next few years. Deposit rates continued into the start of 2017/18 at previous depressed levels due, in part, to a large tranche of cheap financing being made available under the Term Funding Scheme to the banking sector by the Bank of England; this facility ended on 28 February 2018.

The Council's bank, HSBC, increased the interest rate it paid on the sweep facility from 0.10% to 0.35% in response to the Bank Rate increase. There was an average daily total of £6.61m being invested within the HSBC "sweep" deposit account, which earned an average of 0.26% in 2017/18.

10. **<u>Investment Outturn for 2017/18</u>**

Investment Policy – the Council's investment policy is governed by MHCLG guidance, which has been implemented in the annual investment strategy approved by the Council on 22 February 2017. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data. This guidance is enhanced by advice from Link Asset Services.

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Investments held by the Council - the Council maintained a daily average balance of £13.9m of investments during 2017/18. The investments earned an average rate of return of 0.47% which exceeded the target of base rate 0.5% minus 0.2%.

There were a total of 7 market investments made during the financial year, totalling £14m. All investments were for under one year.

The table below shows the maximum amount invested with any of the counterparties at any one time during the period April 2017 to the end of March 2018 against the maximum limits approved in the 2017/18 Treasury Management Strategy.

Counterparties	Maximum Limits £m	Highest level of Investment 2017/18 (£m)
HSBC	15.0	12.8
Bank of Scotland	4.0	4.0
Goldman Sachs	4.0	4.0
Santander UK plc	4.0	4.0

11. **Interest payable on External Borrowing / Interest Receivable on Investments**

The revised budget for the PWLB interest payable on external borrowing for 2017/18 was set at £947,268.

The outturn position was £930,761, due to proactive management of the Councils' cash flows, slippage in capital spending and borrowing requirements, lower PWLB interest rates payable.

The total interest receivable on temporary investments in 2017/18 amounted to £65,808 compared with a budget for the year of £41,845.

FINANCIAL IMPLICATIONS AND BUDGET PROVISION

12. None arising as a direct result of this report.

POLICY IMPLICATIONS

13. All transactions are in accordance with the Council's approved Treasury Policy Statement

DETAILS OF CONSULTATION

14. None

BACKGROUND PAPERS

15. None.

FURTHER INFORMATION PLEASE CONTACT: **Howard Hamilton-Smith**
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