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MERTHYR TYDFIL County Borough Council
Cyngor Bwrdeistref Sirol MERTHYR TUDFUL

FULL COUNCIL REPORT

Date Written	17th November 2015
Report Author	Adele Lewis
Service Area	Finance
Exempt/Non Exempt	Non Exempt
Committee Date	2nd December 2015

To: Mayor, Ladies and Gentlemen

Treasury Management Policy Statement and Annual Investment Strategy 2015/16 In Year Review

1.0 SUMMARY OF THE REPORT

1.1 The In Year Treasury Report outlines the Council's performance for the first six months of 2015/16 in respect of:-

The management of the organisation's cash flows, its banking, money market and capital market transactions.

The effective control of the risks associated with those activities

The pursuit of optimum performance consistent with those risks

2.0 RECOMMENDATION(S) that

2.1 The Treasury Management Policy Statement and Annual Investment Strategy In Year Review Report for 2015/16 be received.

3.0 INTRODUCTION AND BACKGROUND

3.1 The Treasury Management Policy Statement and Annual Investment Strategy for 2015/16 was approved by Council on 25th March 2015. The In Year Review report for 2015/16 is attached at Appendix 1 for Members' attention and is a requirement of the Chartered Institute for Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2011).

3.2 As Members are aware, the Council employs Capita Treasury Solutions Limited as its Treasury Management consultant to give specialist advice on all Treasury Management matters including borrowing and investment requirements. This advice has been followed in producing the Treasury In Year Review Report.

4.0 FINANCIAL IMPLICATION(S)

4.1 Financial information and performance is included within the body of the report.

5.0 SINGLE INTEGRATED PLAN AND SUSTAINABILITY IMPACT SUMMARY

5.1 The Single Integrated Plan & Sustainability Impact Assessment has been completed and the proposals positively impact on a number of aspects of the Corporate Plan and Single Integrated Plan, in particular the financial sustainability of public services. No negative impacts have been identified.

6.0 EQUALITY IMPACT ASSESSMENT

6.1 An Equality Impact Assessment (EqIA) form has been prepared for the purpose of this report. It has been found that a full assessment is not required at this time. The form can be accessed on the Council's website/intranet via the 'Equality Impact Assessment' link.

GARETH CHAPMAN ***CHIEF EXECUTIVE***	***COUNCILLOR PHIL WILLIAMS*** ***CABINET MEMBER FOR GOVERNANCE AND CORPORATE SERVICES***

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<tr><th colspan="4">BACKGROUND PAPERS</th></tr>
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<tr><td>Prudential Indicators – Council Tax 2015/16</td><td>Council 25th March 2015</td><td colspan="2">Accountancy/Intranet Committee Agendas and Minutes</td></tr>
<tr><td>Treasury Management Policy and Annual Investment Strategy 2015/16 (Included within Medium Term Financial Plan Report 2015-16 to 2017-18)</td><td>Council 25th March 2015</td><td colspan="2">Accountancy/Intranet Committee Agendas and Minutes</td></tr>
<tr><td>Treasury Management 2014/15 Working Papers</td><td>April 2015 to October 2015</td><td colspan="2">Accountancy</td></tr>
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Consultation has been undertaken with the Corporate Management Team in respect of each proposal(s) and recommendation(s) set out in this report.

Appendix 1

MERTHYR TYDFIL COUNTY BOROUGH COUNCIL

TREASURY MANAGEMENT POLICY STATEMENT AND ANNUAL INVESTMENT STRATEGY IN YEAR REVIEW 2015/16

1.0 Introduction and Background

1.1 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2011) was adopted by Council on 25th March 2015. The primary requirements of the Code are the: -

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities

- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

- Receipt by the Cabinet / Council of an annual strategy report for the year ahead, an **in year review report** and an annual review report of the previous year.

- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body, Audit Committee / Scrutiny

1.2 Treasury Management in this context is defined as:

"The management of the local authority's cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks. "

This **in year review report** for 2015/16 has been prepared in compliance with CIPFA's Code of Practice and covers:

- an economic update for the first 6 months of 2015/16
- a review of the Treasury Management Policy Statement and Annual Investment Strategy for 2015/16
- a review of the Council's investment portfolio for 2015/16
- a review of the Council's borrowing strategy for 2015/16
- a review of any debt rescheduling undertaken during 2015/16
- a review of compliance with Treasury and Prudential limits for 2015/16

2.0 Economic Update

2.1 Global Economy

2.1.1 The American economy made a strong comeback after a weak first quarters growth at +0.6%, to grow by no less than 3.9% in quarter 2 of 2015. Figures issued on 2nd October were disappointingly weak and confirmed concerns that US Growth is likely to weaken, pushing back expectations of a first rate increase from 2015 into 2016.

2.1.2 In the Eurozone, a quantative easing programme that started in January 2015 appears to have had a positive effect in helping the recovery of consumer and business confidence and had a significant improvement in economic growth. Recent downbeat Chinese and Japanese news has raised questions as to whether the European Central Bank will need to boost its Quantative Easing programme if it is to succeed in significantly improving growth in the Eurozone and getting inflation up from the current level of around zero to its target of 2%.

2.2 UK Economy

2.2.1 The 2014 growth rate was the strongest UK rate since 2006 and the 2015 growth rate is likely to be a leading rate in the G7. The Bank of England August inflation Report had included a forecast for growth to remain around 2.4-2.8% over the next three years. However since the report was issued a further decline in the growth rate to +0.30% in Quarter 4 has been indicated.

2.2.2 The August Bank of England Inflation forecast was notably subdued in respect of inflation, which was forecast to barely get back to the 2% target within the 2-3 year time horizon. There are considerable risks around whether inflation will rise in the near future as strongly as had been previously expected; this will make it more difficult for the central banks to raise rates as soon as was being forecast.

2.3 Sector's Interest Rate Forecast

2.3.1 It is evident from Table 1 that UK Bank Rate is expected to rise from 0.5% to 0.75% is forecast in the 2nd quarter of 2016, beginning a trend of increases thereafter.

Table 1 – Interest Rate Forecasts

	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18
Bank rate	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.50%	1.50%	1.75%	1.75%
5yr PWLB rate	2.40%	2.50%	2.60%	2.80%	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%
10yr PWLB rate	3.00%	3.20%	3.30%	3.40%	3.50%	3.70%	3.80%	3.90%	4.00%	4.10%	4.20%
25yr PWLB rate	3.60%	3.80%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.60%	4.60%
50yr PWLB rate	3.60%	3.80%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.60%	4.60%

3.0 Treasury Management Policy Statement and Annual Investment Strategy Update

3.1 The Treasury Management Policy Statement and Annual Investment Strategy for 2015/16 was approved by Council on 25th March 2015.

3.2 The Council will aim to achieve the optimum return (yield) on investments commensurate with the proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term, only investing with the top UK Banks and Building Societies and other UK Local Authorities.

3.3 Investments and borrowing during the first six months of the year have been in line with the strategy with no deviations from the strategy.

3.4 As outlined in Section 2, there is still considerable uncertainty and volatility in the financial and banking market, both globally and in the UK. In this context, it is considered that the strategy approved on 25th March 2015 is still fit for purpose in the current economic climate.

4.0 Investment Portfolio 2015/16

4.1 In accordance with CIPFA's Code of Practice, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite.

4.2 Outstanding investments at 31st March 2015 totalled £5.8 million at an average interest rate of 0.43%. New investment for the first 6 months of 2015/16 is as Table 2 and was kept short-term average of 2 to 3 months.

Table 2 – Analysis of Investments 2015/16

Date	Invested £million	Average Interest Rate %
April 2015	6.30	0.42
May 2015	6.50	0.47
June 2015	5.30	0.43
July 2015	7.00	0.38
August 2015	8.00	0.37
September 2015	3.50	0.38
	36.60	**0.41**

No investments remained outstanding at 30th September 2015.

4.3 Investment income of £11,622 was realised for the first 6 months of the financial year, 1st April 2015 to 30th September 2015, against budgeted investment income of £12,000.

5.0 External Borrowing 2015/16

5.1 The Authority has undertaken short-term borrowing (2 to 3 months) of £21.31 million during the first 6 months of 2015/16 with other UK local authorities. A summary analysis is included in Table 3.

Table 3 – Analysis of Borrowing 2015/16

Date	Advance £million	Average Interest Rate %
April 2015	3.00	0.30
May 2015	1.06	0.33
June 2015	5.00	0.37
July 2015	2.50	0.32
August 2015	5.00	0.35
September 2015	4.75	0.30
Total	**21.31**	**0.33**

Short-term debt of £4.75 million remained unpaid at 30th September 2015.

5.2 Interest payments in relation to short-term borrowing for the 1st April 2015 to 30th September 2015 totalled £5,584 against budgeted interest of £7,500.

6.0 Debt Rescheduling

6.1 Debt rescheduling opportunities have been limited in the current economic climate and consequent structure of interest rates. As a result no debt rescheduling was undertaken during the first six months of 2015/16 with none anticipated for the remaining six months of the financial year.

7.0 Compliance with Treasury and Prudential Limits

7.1 During the financial year to date the Council has operated within the Treasury Limits and Prudential Indicators set out in the Council's Treasury Management Policy Statement and Annual Investment Strategy 2015/16 reported to Council 25th March 2015. The Prudential and Treasury Indicators previously reported are shown in Appendix 2.

Appendix 2

The Prudential Code for Capital Finance in Local Authorities

The Prudential Indicators

Prudential Indicators are the mechanism by which the Authority is able to demonstrate that its capital investment decisions are affordable, prudent and sustainable and are designed to support and record local decision-making.

The recommended Prudential Indicators for the Council for the financial years 2015/16 to 2017/18 are disclosed below. I would advise Council that the financial forecasts are made on the basis of best information available at this time and by making reasonable assumptions where significant elements of uncertainty existed. Furthermore, the three-year forecasts are rolling scenarios not fixed for three years.

1. Ratio of Financing Costs to Net Revenue Stream

This indicator is specifically related to the affordability of capital investment decisions addressing the revenue implications of the Authority's financial strategy. In determining the indicators, recommended new borrowing to finance desired future capital expenditure is taken into account.

	Projected 2014/15	**Estimate 2015/16**	**Estimate 2016/17**	**Estimate 2017/18**
Prudential Indicator	7%	7%	7%	7%

2. Estimates of the Incremental Impact of Capital Investment Decisions on the Council Tax

This indicator identifies the incremental impact to the Council Tax from the capital expenditure proposals, particularly changes in borrowing requirements, for 2015/16 and the following two years. The 2015/16 incremental impact is included in the overall recommended Council Tax increase for Merthyr Tydfil County Borough Council for 2015/16 of 4.50%. This is a fundamental indicator of affordability.

Prudential Indicator	**Estimate 2015/16**	**Estimate 2016/17**	**Estimate 2017/18**
Impact on Council Tax	£5.81	£13.63	£18.62

3. Gross Debt and the Capital Financing Requirement

In order to ensure that over the medium term debt will only be for a capital purpose, the Authority should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence.

As evident from the table below debt is not projected to exceed the capital financing requirement.

Description	Projected 31/03/15 £'000	Estimate 31/03/16 £'000	Estimate 31/03/17 £'000	Estimate 31/03/18 £'000
Capital Financing Requirement	83,212	89,852	92,324	93,303
Debt	81,524	79,598	81,729	84,104
Prudential Indicator	**1,688**	**10,254**	**10,595**	**9,199**

4. Capital Expenditure

The capital expenditure projected outturn for 2014/15 and the estimates of capital expenditure to be incurred for 2015/16 and the following two years are as follows.

	Projected 2014/15 £'000	Estimate 2015/16 £'000	Estimate 2016/17 £'000	Estimate 2017/18 £'000
Prudential Indicator	31,961	35,162	62,105	10,017

The capital expenditure projections for the next three years are derived after taking into account affordable, prudent and sustainable borrowing levels after estimating the availability of capital finance from capital receipts, grants and external contributions. Excess borrowing will either lead to increased Council Tax or reductions in service provision.

5. Capital Financing Requirement

Estimates of the end of year capital financing requirement for the Authority for the current and next three financial years are:

	Projected 31/03/15 £'000	Estimate 31/03/16 £'000	Estimate 31/03/17 £'000	Estimate 31/03/18 £'000
Prudential Indicator	83,212	89,852	92,324	93,303

The capital financing requirement measures the Authority's underlying need to borrow for a capital purpose.

6. Authorised Limit for External Debt

The Council's authorised limits for its external debt gross of investments for the next three financial years are as follows. These limits separately identify borrowing from other long-term liabilities.

Authorised Limit	**Estimate 2015/16 £'000**	**Estimate 2016/17 £'000**	**Estimate 2017/18 £'000**
Borrowing	97,816	100,053	102,547
Other Long-term Liabilities	500	500	500
Prudential Indicator	**98,316**	**100,553**	**103,047**

These authorised limits are consistent with the Authority's current commitments, existing plans and the proposals in this budget report for capital expenditure and financing, and with its approved treasury management policy statement and practices. I can confirm that they are based on the estimate of most likely, prudent but not worst case scenarios, with in addition sufficient headroom over and above this to allow for operational management, for example unusual cash movements.

Capital expenditure plans, estimates of the capital financing requirement and estimates of cash flow requirements for all purposes have been taken into account.

The Council is asked to approve these limits and to delegate authority to the Chief Finance Officer for the effective management and monitoring of the authorised limit.

In taking its decisions on this budget report, the Council is asked to note that the authorised limit determined for 2015/16 will be the statutory limit determined under section 3(1) of the Local Government Act 2003 – "A local authority shall determine and keep under review how much money it can afford to borrow".

7. Operational Boundary for External Debt

The proposed operational boundary for external debt is based on the same estimates as the authorised limit but reflects directly the Chief Finance Officer's estimate of the most likely, prudent but not worst case scenario, without the additional headroom included within the authorised limit to allow for example for unusual cash movements, and equates to the maximum of external debt projected by this estimate.

The operational boundary represents a key management tool for in year monitoring by the Chief Finance Officer and is disclosed below with borrowing and other long term liabilities separately identified.

Operational Boundary	Estimate 2015/16 £'000	Estimate 2016/17 £'000	Estimate 2017/18 £'000
Borrowing Other Long-term Liabilities	93,158 500	95,289 500	97,664 500
Prudential Indicator	**93,658**	**95,789**	**98,164**

The Council is asked to approve these limits and to delegate authority to the Chief Finance Officer for the effective management and monitoring of the operational boundary.

8. Actual External Debt

The Council's projected actual external debt, subject to audit, at 31st March 2015 is £81.168 million.

External Debt	Projected 2014/15 £'000
Borrowing Other Long-term Liabilities	80,584 584
Prudential Indicator	**81,168**

It should be noted that actual external debt is not directly comparable to the authorised limit and operational boundary, since the actual external debt reflects the position at one point in time.

9. Adoption of the CIPFA Code of Practice for Treasury Management in the Public Services

The Authority has adopted the CIPFA Code of Practice and will be reporting its Treasury Management Policy Statement for the 2015/16 financial year to Council of 25 March 2015.

Treasury Indicators

10. Interest Rate Exposures

While fixed-rate borrowing and investment can contribute significantly to reducing the uncertainty surrounding future interest rate scenarios, the pursuit of optimum performance may justify, or even demand, retaining a degree of flexibility through the use of variable interest rates on at least part of a treasury management portfolio. This is a best practice approach to treasury management ensuring effective management and control of risk.
It is recommended that the Council sets an upper limit on its fixed interest rate exposures for 2015/15, 2016/17 and 2017/18 of 99% of its net interest payable on borrowing.

It is further recommended that the Council sets an upper limit on its variable interest rate exposures for 2015/16, 2016/17 and 2017/18 of 12% of its net interest payable on borrowing.

This means that the Chief Finance Officer will manage fixed interest rate exposures within the range 88% to 99% and variable interest rate exposures within the range 1% to 12%. The estimated net interest payable in respect of each range is shown in the following Table.

Prudential Indicator	Estimate 2015/16 £'000	Estimate 2016/17 £'000	Estimate 2017/18 £'000
Fixed Rates			
88%	4,529	4,384	4,284
99%	5,096	4,932	4,819
Variable Rates			
1%	51	50	49
12%	618	598	584

When interest rates are considered to be relatively low then the policy is to borrow at fixed interest rates taking advantage of any potential future market increases.

11. Maturity Structure of Borrowing

This indicator is designed to be a control over an authority having large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates.

This is the amount of projected borrowing that is maturing in each period as a percentage of total projected borrowing for fixed rate and Variable rate debt.

It is recommended that the Council sets upper and lower limits for the maturity structure of its borrowings as follows:

Fixed debt

Period	Upper Limit	Lower Limit
Under 12 months	4%	0%
12 months and within 24 months	4%	0%
24 months and within 5 years	15%	0%
5 years and within 10 years	25%	0%
10 years and above	52%	0%

Variable debt

Period	Upper Limit	Lower Limit
Under 12 months	100%	0%
12 months and within 24 months	0%	0%
24 months and within 5 years	0%	0%
5 years and within 10 years	0%	0%
10 years and above	0%	0%

The 2011 Code states for LOBO Loans the Maturity date is now deemed to be the next call date.

12. Total Principal Sums Invested for Periods Longer than 364 Days

There are no proposals for the Council to invest sums for periods longer than 364 days.

The purpose of this Prudential Indicator is for the Authority to contain its exposure to the possibility of loss that might arise as a result of its having to seek early repayment or redemption of principal sums invested.