The Vale of Glamorgan Council

Cabinet Meeting: 31 July, 2017

Report of the Leader

Treasury Management

Purpose of the Report

1. To present to Cabinet the annual review report on Treasury Management 2016/17.

Recommendation

1. That Cabinet accept the annual report on Treasury Management 2016/17 and that the report be referred to Council for approval.

Reason for the Recommendation

1. To accept and refer the report to Council.

Background

2. In March 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, a mid year report, and an annual report after the end of each financial year.

3. This annual treasury management report has been prepared as required and covers:

- the economy / interest rates in 2016/17;
- the strategy for 2016/17;
- the borrowing outturn for 2016/17;
- investment outturn for 2016/17; and
- compliance with treasury limits and Prudential Indicators;

The Economy / Interest Rates in 2016/17

4. The following information has been prepared by the Authority's Treasury Management advisors and sets out the changing conditions under which Treasury Management operations were carried out.

5. Politically, 2016/17 was an exceptional twelve month period during which the UK voted to leave the European Union and there was an election for the 45th President

of the USA. Uncertainty over the outcome of the US presidential election, the UK's future relationship with the EU and the slowdown witnessed in the Chinese economy in early 2016 all resulted in significant market volatility during the year.

6. UK inflation had been subdued in the first half of 2016 as a consequence of weak global price pressures, past movements in sterling and restrained domestic price growth. However the sharp fall in the Sterling exchange rate following the EU referendum had an impact on import prices which, together with rising energy prices, resulted in CPI rising from 0.3% year on year in April 2016 to 2.3% year on year in March 2017.

7. The referendum's outcome also prompted a decline in household, business and investor confidence. The repercussions on economic growth were judged by the Bank of England to be sufficiently severe to prompt its Monetary Policy Committee (MPC) to cut the Bank Rate to 0.25% in August and embark on further gilt and corporate bond purchases as well as provide cheap funding for banks via the Term Funding Scheme to maintain the supply of credit to the economy.

8. Despite growth forecasts being downgraded, economic activity was fairly buoyant and GDP grew 0.6%, 0.5% and 0.7% in the second, third and fourth calendar quarters of 2016 respectively. The labour market also proved resilient, with the International Labour Organisation (ILO) unemployment rate dropping to 4.7% in February, its lowest level in 11 years.

9. Following the referendum result, gilt yields fell sharply across the maturity spectrum on the view that the Base Rate would remain extremely low for the foreseeable future. After September there was a reversal in longer-dated gilt yields which moved higher, largely due to the MPC revising its earlier forecast that the Base Rate would be dropping to near 0% by the end of 2016.

10. Money market rates for overnight and one week periods remained low since the Base Rate was cut in August. 1- and 3-month LIBID rates averaged 0.36% and 0.47% respectively during 2016-17. Rates for 6- and 12-months increased between August and November, only to gradually fall back to August levels in March and averaged 0.6% and 0.79% respectively during 2016-17.

11. Various indicators of credit risk reacted negatively to the result of the referendum on the UK's membership of the European Union. Fitch and Standard & Poor's downgraded the UK's sovereign rating to AA. Fitch, S&P and Moody's have a negative outlook on the UK. Moody's has a negative outlook on those banks and building societies that it perceives to be exposed to a more challenging operating environment arising from the 'leave' outcome.

Treasury Management Strategy 2016/17

12. The Section 151 Officer continued to adopt a cautious approach with respect to Treasury Management operations. The Council's primary objectives for the management of its investments are to give priority to the security and liquidity of its funds before seeking the best rate of return. This being the case the Authority placed the majority of funds available for investment purposes with other local authorities. These investments attract a slightly more favourable rate of return than investing with the UK government, but still give priority to the security of funds invested.

13. Funds not placed with other Local Authorities were placed in the 'Debt Management Account Deposit Facility' (DMADF) as these deposits are guaranteed by the British

Government. However, these deposits attract a lower return than those available from placement of funds with either local authorities or commercial banks.

14. The Council's primary objective for the management of its debt is to ensure its long term affordability. The majority of its loans have therefore been borrowed from the Public Works Loan Board at long term fixed rates of interest. In 2016/17 the Council continued to finance a significant proportion of its capital expenditure from internal resources. The potential reduction of the Council's investment balances at times of elevated credit risk was still considered the most prudent option available to the Authority throughout 2016-2017.

15. Council approved the Treasury Management Strategy for 2016/17 at its meeting on the 1st March 2016, minute no. 882.

16. The Section 151 Officer advises that all treasury management activity undertaken during the financial year complied with the amended approved strategy, the CIPFA Code of Practice and the relevant legislative provisions.

Borrowing Outturn 2016/17

17. During 2016/17 £9,907,863 of internal funds was used in the financing of capital expenditure. An average rate of interest was charged to reflect the use of capital resources. The total charges for interest and principal including for prudential borrowing during the year 2016/17 were £7,946,734 and £6,179,038 respectively.

18. For all borrowing excluding loans that are advanced under the Local Government Borrowing Initiative an original estimate of 3.89% revised to 3.95% had been included in the estimates for 2016/17. The actual rate was 4.08%.

19. The Authority internally financed prudential borrowing totalling £6,537,863. This new borrowing comprised of 2 new loans. An education "21st Century School" investment programme loan for £1,137,863 charged at a rate of 4.04% and a "Welsh Housing Quality Standard" (WHQS) loan for £5,400,000 charged at a rate of 4.08%. The total charge for interest and principal for 2016/2017 on prudential borrowing was £3,470,477 and £1,797,794 respectively.

20. The Council’s external debt as at the 31st March 2017 (excluding accrued interest) was £157.199 million (1st April 2016 £159.411 million). This can be summarised as follows:

	Opening Balance 1st April 2016	**Received**	**Repaid**	**Closing Balance 31st March 2017**
	£’000	£’000	£’000	£’000
P.W.L.B.	151,211	0	-2,212	148,999
Market Loans	6,000	0	0	6,000
Concessionary	2,100	0	0	2,100
Temporary Loans	100	0	0	100
Total	**159,411**	**0**	**-2,212**	**157,199**

- Loans borrowed from the Public Works Loan Board (PWLB) are intended to assist local authorities in meeting their longer term borrowing requirements. The Authority did not borrow any new loans from the PWLB during 2016-2017, opting to fund from internal resources. The average interest rate on all the Authority's outstanding PWLB debt has moved over the course of the year from 4.8204% to 4.7606%.

- Market loans represent those non-PWLB loans that are repayable at least 1 year or more from the date they are advanced. The debt is a market loan, £2,000,000 of which will mature on the 8th November 2021 and £4,000,000 will mature on the 23rd February 2054. The average interest rate on the Authority's outstanding market loans is 5.322%
- The Concessionary Loan was advanced to the Authority by the Welsh Assembly Government on the 1st April 2015 for a period of 10 years. The loan will mature on the 31st March 2025 and is interest free.
- Temporary Loans represent loans that have no fixed maturity date. Current loans have been borrowed from The Vale of Glamorgan Welsh Church Act Fund. Interest is calculated on a monthly basis using the "Average 7 Day Rate". The interest rates payable on the Authority's outstanding temporary loans ranged from 0.26% to 0.51% during 2016/17.

Investment Outturn for 2016/17

21. Internally Managed Investments – The Authority manages investments in-house and is able to invest with those institutions which meet the minimum credit rating criteria and are included on the approved lending list as laid out in the investment strategy. The Authority currently invests short term for a range of periods from overnight to 364 days, dependent on its cash flows, its interest rate view and the interest rates/ periods on offer.

22. Investment movements for 2016/17 (excluding accrued interest) are summarised as follows:-

	Opening Balance 1st April 2016	**Invested**	**Repaid**	**Closing Balance 31st March 2017**
	£'000	£'000	£'000	£'000
Debt Management Account Deposit Facility	30,600	1,785,950	-1,812,300	4,250
Local Authorities	48,000	195,100	-177,600	65,500
Total	**78,600**	**1,981,050**	**-1,989,900**	**69,750**

23. The continuing market uncertainties resulted in the majority of available funds still being invested cautiously either in the Debt Management Account Deposit Facility (DMADF) or with Local Authorities. The Authority this year favoured deposits with local authorities as these investments attracted a slightly more favourable return without any increase in risk to the principal sums invested.

24. Debt Management Account Deposit Facility - The Authority continued to place a portion of all surplus funds in the DMADF, which is guaranteed by the British Government. The maturity dates of these investments ranged from overnight to a maximum period of 6 months. The Authority made a return of £59,902 during 2016-2017. The rate of interest receivable on these investments was reviewed 3 times during the year. A rate of 0.25% was received for the period 1st April 2016 to 4th August 2016, 0.15% for the period 5th August 2016 to 23rd February 2017 and 0.10% for the period 24th February 2017 to 31st March 2017.

25. Local Authorities - During the year deposits were placed with local authorities. The Authority made a return on these investments of £243,158 at a rate of 0.4044%

26. The overall return on investments for 2016/17 was 0.3356%.

27. The Section 151 Officer will continue to keep the borrowing / investment strategy under review.

Treasury Limits and Prudential Indicators

28. The Council is asked to note the Prudential Indicators shown in appendix A.

Resource Implications (Financial and Employment)

29. The resources implications are detailed in the report.

Sustainability and Climate Change Implications

30. There are no sustainability and climate change implications as a direct result of this report.

Legal Implications (to Include Human Rights Implications)

31. As set out in this report.

Crime and Disorder Implications

32. There are no crime and disorder implications as a direct result of this report.

Equal Opportunities Implications (to include Welsh Language issues)

33. There are no equal opportunity implications as a direct result of this report.

Corporate/Service Objectives

34. To provide sound financial and reliable advice in relation to all issues affecting the Council

Policy Framework and Budget

35. The report will be forwarded to Full Council for approval

Consultation (including Ward Member Consultation)

36. The appropriate Chief Officers have been consulted on this report. This report does not require Ward Member consultation.

Relevant Scrutiny Committee

37. Corporate Performance and Resources

Background Papers

None

Contact Officer

Gemma Jones Principal Accountant

Officers Consulted

All appropriate Chief Officers have been consulted on the contents of this report.

Responsible Officer:

Carys Lord
Section 151 Officer