Committee and Date
Cabinet 30 July 2014
Audit Committee 18 September 2014
Council 25 September 2014

ANNUAL TREASURY REPORT 2013/14

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1. Summary

1.1. The report informs members of treasury activities for Shropshire Council for 2013/14, including the investment performance of the internal treasury team to 31 March 2014. The internal treasury team outperformed their investment benchmark by 0.3% in 2013/14 and performance for the last three years is 0.5% per annum above benchmark. Treasury activities during the year have been within approved prudential and treasury indicators set and have complied with the Treasury Strategy.

1.2. During 2013/14 the performance of the Treasury Team delivered an under spend of £1.319 million compared to budget as highlighted in paragraph 10.7 of this report. This under spend helped the Council to achieve an overall under spend at the end of the financial year.

1.3. The claim for the £1 million deposit placed by Bridgnorth District Council with the Icelandic Bank, Landsbanki has now been sold through a competitive auction process. The sale means that the Council has recovered 92% of the amount that was originally deposited. The sale of the claim represents a clean break and the Council is no longer a creditor of Landsbanki.

2. Recommendations

2.1. Members are asked to accept the position as set out in the report.

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3. Risk Assessment and Opportunities Appraisal

3.1. The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998.

3.2. There are no direct environmental, equalities or climate change consequences arising from this report.

3.3. Compliance with the CIPFA Code of Practice on Treasury Management, the Council’s Treasury Policy Statement and Treasury Management Practices and the Prudential Code for Capital Finance together with the rigorous internal controls will enable the Council to manage the risk associated with Treasury Management activities and the potential for financial loss.

4. Financial Implications

4.1. The Council makes assumptions about the levels of borrowing and investment income over the financial year. Reduced borrowing as a result of capital receipt generation, or delays in delivery of the capital programme will both have a positive impact of the council's cash position. Similarly, higher than benchmarked returns on available cash will also help the Council's financial position. For monitoring purposes, assumptions are made early in year about borrowing and returns based on the strategies agreed by Council in the preceding February. Performance outside of these assumptions result in increased or reduced income for the Council.

4.2. The 2013/14 performance is above benchmark for the reasons outlined in paragraph 10.7 of this report and has delivered additional income of £1.319 million which has been reflected in the final Revenue Monitor report for 2013/14.

5. Background

5.1. The Council defines its treasury management activities as "the management of the authority's investments and 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".

5.2. The Council is required through regulations issued under the Local Government Act 2003 to produce an annual treasury report reviewing treasury management activities and the actual prudential and treasury indicators for 2013/14. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities.

5.3. Changes in the regulatory environment place a much greater onus on members for the review and scrutiny of treasury management policy and activities. Minimum reporting requirements are that the Council should receive the following reports:

- An annual treasury strategy in advance of the year.
- A mid-year treasury update report.
- An annual report following the year describing the activity compared to the strategy.

5.4. The CIPFA Code of Practice on Treasury Management states that these reports should be scrutinised by a nominated committee and members should be trained on treasury management activities in order to support them in their scrutiny role. These reports were scrutinised by the Audit

Committee before they were reported to full Council for approval. Members also received training on treasury management issues to support their scrutiny role by completing the CIPFA treasury management self-assessment and further Member training was undertaken in November 2013 in conjunction with our Treasury Advisor, Capita Asset Services.

5.5. In addition to the minimum reporting requirements, the Director's and Cabinet also receive quarterly treasury management update reports for information.

5.6. The Treasury Strategy for 2013/14 was approved by Council in February 2013, the mid-year treasury update report was approved by Council in December 2013. This Annual Report sets out our actual treasury performance for the year and shows how the actual treasury performance varied from our estimates and planning assumptions.

6. Borrowing Strategy for 2013/14

6.1. The borrowing strategy for the year continued to be funding the Council's long term borrowing requirement at advantageous rates. Short term finance from internal balances would be used in the interim pending favourable market conditions for long term funding.

6.2. Short term Public Works Loan Board (PWLB) rates were expected to be significantly cheaper than longer term borrowing rates during the year therefore borrowing in the 10 year period early on in the financial year when rates were expected to be at their lowest would be considered. Variable rate borrowing was also expected to be cheaper than long term fixed rate borrowing throughout the year.

6.3. An alternative strategy was to defer any new borrowing as long term borrowing rates were expected to be higher than investment rates during the year. This would maximise savings in the short term and also have the added benefit of running down investments which would reduce credit risk. Short term money market borrowing was not used during the year.

7. Borrowing outturn for 2013/14

7.1. The Treasury Team take advice from its external treasury advisor, Capita Asset Services, on the most opportune time to borrow. Movements in rates during 2013/14 are shown in the graph at Appendix A.

7.2. Members have previously been advised of the unexpected change of policy on PWLB lending arrangements in October 2010 following the Comprehensive Spending Review. This resulted in an increase in all new borrowing rates of between 0.75 – 0.85%, without an associated increase in early redemption rates. This made new borrowing more expensive and repayment relatively less attractive.

7.3. The table below shows PWLB borrowing rates for a selection of maturity periods. The table also shows the high and low points in rates during the year, average rates during the year and individual rates at the start and the end of the financial year.

	4.5 – 5yrs	9.5 – 10yrs	24.5 – 25 yrs	49.5 – 50 yrs
01/04/2013 31/03/2014	1.75% 2.50%	2.84% 3.66%	4.08% 4.45%	4.23% 4.48%
High	2.97%	4.10%	4.67%	4.70%
Low	1.61%	2.58%	3.78%	4.07%
Average	2.47%	3.58%	4.43%	4.47%
High date	27/12/2013	02/01/2014	10/09/2013	10/09/2013
Low date	15/04/2013	19/04/2013	19/04/2013	03/05/2013

7.4. Following discussions with Capita, as general fund borrowing rates were significantly higher than investment rates during the year it was agreed that if any new borrowing was required during the year it would be deferred in order to maximise savings in the short term and reduce credit risk by reducing investments. Due to a review of the Capital Programme no new external borrowing was required in 2013/14.

7.5. The Council's total debt portfolio at 31 March 2014 is set out below:-

Type of Debt	Balance £m	Average Borrowing Rate 2013/2014
General Fund Fixed rate – PWLB	210.22	5.55%
HRA Fixed rate - PWLB	83.35	3.51%
Fixed rate – Market	49.20	4.10%
Variable rate	0	N/A

7.6. The average borrowing rate for the total portfolio (PWLB and Market) has remained the same at 5% in 2012/13 and 2013/14 due to no new borrowing being undertaken. The maturity profile of the debt is evenly spread to avoid large repayments in any one financial year. The average debt period for PWLB loans is 22 years, market loans have an average debt period of 56 years. The total debt portfolio has a maturity range from 1 year to 64 years.

7.7. The Treasury Strategy allows up to 15% of the total outstanding debt to mature in any one year. It is prudent to have the Council's debt maturing over many years so as to minimise the risk of having to re-finance when interest rates may be high. The actual debt maturity profile is within these limits (Appendix B).

8. Debt rescheduling

8.1. No debt restructuring was undertaken during 2013/14. The introduction of a differential in PWLB rates on the 1 November 2007, which was compounded further since a policy change in October 2010 as outlined above, has meant that large premiums would be incurred if debt restructuring was undertaken which cannot be justified on value for money grounds.

8.2. Although these changes have restricted debt restructuring, the current debt portfolio is continually monitored in conjunction with external advisers in the light of changing economic and market conditions to identify opportunities for debt rescheduling. Debt rescheduling will only be undertaken:

- To generate cash savings at minimum risk.
- To help fulfil the Treasury Strategy.
- To enhance the balance of the long term portfolio by amending the maturity profile and/or volatility of the portfolio.

9. Investment Strategy for 2013/14

9.1. Our treasury advisor originally felt when the strategy was approved by Council in February 2013 that the bank rate would remain at its historically low level of 0.50% throughout the year with the first rise to 0.75% not expected until March 2015. During the year their interest rate forecast was reviewed and their updated forecast was approved by Council in December 2013 as part of the mid-year report. Their revised forecast was that the bank rate would remain at 0.50% until September 2016.

9.2. In 2013/14 investment of surplus cash was managed by the internal treasury team. The strategy for the in-house team was influenced by the need to keep funds relatively short for cash flow purposes. Lending continued to be restricted to UK banks, one overseas bank, one Building Society, Nationalised and Part Nationalised Banks, UK Government and other Local Authorities in line with the Council's policy on creditworthiness which was approved in the Annual Investment Strategy.

10. Investment Outturn 2013/14

10.1 The tight monetary conditions following the 2008 financial crisis continued through 2013/14 with little material movement in shorter term deposit rates. Bank rate remained at its historical low of 0.5% throughout the year and has now remained unchanged for five years. Market expectations of the start of monetary tightening remained the same during the year with the first increase in the Bank Rate not expected until the start of 2015 at the earliest. The Government's Funding for Lending Scheme resulted in deposit rates remaining depressed during the whole of the year.

10.2 Economic growth (GDP) in the UK was virtually flat during 2012/13 but surged strongly during 2013/14. Consequently there was no additional quantitative easing during 2013/14 and the Bank Rate ended the year unchanged at 0.5% for the fifth successive year. While CPI inflation had remained stubbornly high and substantially above the 2% target during 2012, by January 2014 it had, at last fallen below the target rate to 1.9% and then fell further to 1.7% in February. It is expected to remain below the target rate for the next two years ahead.

10.3 The EU sovereign debt crisis subsided during the year and confidence in the ability of the Eurozone to remain intact increased substantially. Perceptions of counterparty risk improved after the European Central Bank (ECB) statement in July 2012 that it would do "whatever it takes" to support the struggling Eurozone countries. This led to a return of confidence in its banking system which continued into 2013/14. However, this is not to say that the problems of the Eurozone, or its banks, have ended as the Eurozone faces the likelihood of weak growth over the next few years at a time when the total size of government debt for some nations is likely to continue rising. Continued stress tests of the Eurozone banks could also reveal some areas of concern.

10.4 The Funding for Lending Scheme, announced in July 2012, has resulted in a flood of cheap credit being made available to banks and this has resulted in money market investment rates falling drastically in the second half of 2012 and continuing into 2013/14.

10.5 To counter the historically low investment rates, and following advice from Capita, use was made of direct deals with main UK banks which were part nationalised for various periods from three months to one year. Direct deals offered substantially enhanced rates over the equivalent rates available through brokers. This provided opportunities to lock into higher, long term rates at times when it was thought they offered substantial enhancement over short term benchmark rates. Due to the enhanced market rates over bank rate this resulted in the total portfolio outperforming the benchmark. Continued use of instant access accounts with Natwest, HSBC and Svenska Handelsbanken was also used as these accounts offered both instant access to funds and paid a rate which was higher than placing short term deposits through brokers.

10.6 Movements in short term rates through the year are shown in the graph at Appendix A.

10.7 Throughout the year the level of interest rates and average investment balances were higher than budgeted. This resulted in the internal treasury team achieving a higher level of interest on revenue balances than budgeted. This £248,929 surplus was in addition to an under-spend on debt charges of £1,070,328 due to no long term general fund borrowing being undertaken in 2013/14. The total £1.319 million under spend helped the Council to achieve an overall under spend at the end of the financial year.

10.8 At 31 March 2014 the allocation of the cash portfolio was as follows:

	£m
• In-house short dated deposits for cash flow management	82.6
• In-house long dated deposits (up to 1 year)	24.1
• Other Local Authorities	3.0
Total	**109.7**

10.9 The following table shows the average return on cash investments for the internal treasury team during the year and for the last 3 years to 31 March 2014. Recognising the need to manage short term cash flow requirements, the target for the internal team is the Local Authority 7 day deposit rate.

	Return 2013/14	Return 3 years to 31 March 2014
	%	% p.a
Internal Treasury Team	0.6	0.8
Benchmark (Local Authority 7 Day LIBID rate)	0.3	0.3

10.10 The conclusions to be drawn from the table are:

- During 2013/14 the internal treasury team outperformed their benchmark by 0.3%.
- Over the 3 year period the internal team's performance has been 0.5% per annum above the benchmark.

11. Landsbanki Deposit Update

11.1 The claim for the £1 million deposit placed by Bridgnorth District Council with the Icelandic Bank, Landsbanki has now been sold through a competitive auction process. The sale means that the Council has recovered 92% of the amount that was originally deposited. The sale of the claim represents a clean break and the Council is no longer a creditor of Landsbanki.

12. Compliance with Treasury Limits and Prudential Indicators

12.1 All borrowing and lending transactions undertaken through the year have complied with the procedures and limits set out in the Council's Treasury Management Practices and Treasury Strategy. In addition, all investments made have been within the limits set in the approved counterparty list. No institutions, in which investments were made, showed any difficulty in repaying investments and interest in full during the year.

12.2 Appendix C shows the Prudential Indicators approved by Council as part of the 2013/14 and 2014/15 (revised estimate) Treasury Strategies compared with the actual figures for 2013/14. In summary, during 2013/14 treasury activities have been within the prudential and treasury limits set in the Treasury Strategy.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)

Council, 28 February 2013, Treasury Strategy 2013/14.
Council, 19 December 2013, Treasury Strategy 2013/14 Mid-Year Review.
Council, 27 February 2014, Treasury Strategy 2014/15.
Cabinet, 24 July 2013, Treasury Management Update Quarter 1 2013/14.
Cabinet, 13 November 2013, Treasury Management Update Quarter 2 2013/14.
Cabinet, 12 February 2014, Treasury Management Update Quarter 3 2013/14.
Cabinet, 04 June 2014, Treasury Management Update Quarter 4 2013/14.

Cabinet Member:
Mike Owen, Portfolio Holder

Local Member
N/A

Appendices
A. Movement in Interest Rates 2013/14
B. Debt Maturity Profile as at 31 March 2014
C. Prudential Indicators 2013/14