| REPORT TO | DATE OF MEETING |
|---|---|
| Governance Committee | 28 June 2017 |

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SOUTH RIBBLE BOROUGH COUNCIL
forward with South Ribble

| SUBJECT | PORTFOLIO | AUTHOR | ITEM |
|---|---|---|---|
| Treasury Management Annual Report 2016/17 | Finance & Resources | M L Jackson | 7 |

## SUMMARY AND LINK TO CORPORATE PRIORITIES

The current regulatory environment concerning treasury management places a greater onus on members to scrutinise treasury policy and activity. To enable that, each year the Council is required to consider, as a minimum, three treasury reports. These consist of an annual strategy statement in advance of the year (Council 2 March 2016), a mid-year review of that strategy (Governance Committee 21 September 2016), and finally this out-turn report.

The key messages within this report are that Prudential and Treasury Indicators were complied with; and that the return on investments totalled 0.57% which exceeded the 7-day LIBID benchmark of 0.21%.

## RECOMMENDATIONS

Governance Committee is asked to note the report.

## DETAILS AND REASONING

The Treasury Strategy for 2016/17 to 2018/19 was submitted to Cabinet on 10 February 2016. The overall strategy included Prudential Indicators, the Treasury Management Strategy, the Annual Investment Strategy, and the Annual Minimum Revenue Provision (MRP) Policy Statement, all of which were approved by Council on 2 March 2016.

Revised Prudential and Treasury Indicators for 2016/17 were included in the Treasury Strategy 2017/18 to 2019/20, which was approved by Council on 1 March 2017. Where relevant, comparisons with 2016/17 indicators in this report are to those approved most recently.

Prudential Indicator: Capital Expenditure and Financing 2016/17

A comprehensive report on the Capital Programme provisional outturn for 2016/17 has been submitted separately to Governance Committee on this agenda. Total capital expenditure in the year was £2.353m, and expenditure by category and the proposed source of financing is presented in the Capital Financing Requirement table.

Prudential Indicator: The Capital Financing Requirement (CFR)

The Capital Financing Requirement (CFR) is a measure of the capital expenditure incurred by the Council which is still to be paid for. Such expenditure will currently be met by borrowing or by temporary use of internal cash balances. Ultimately, however, it has to be paid for and will be a charge to Council Tax payers. The Minimum Revenue Provision (MRP) charged to the Council's revenue budget each year is based on the CFR. Its impact on reducing the CFR is shown in the following table:

| Capital Expenditure and Financing | 2016/17 £'000 |
|---|---|
| **Opening Capital Financing Requirement** | **5,902** |
| Capital investment | |
| Property, Plant and Equipment | 1,730 |
| Investment property | (6) |
| Intangible Assets | 79 |
| Revenue Expenditure Funded from Capital under Statute | 550 |
| Total capital investment | 2,353 |
| Sources of finance | |
| Capital Receipts | (21) |
| Government Grants and Other Contributions | (1,026) |
| Sums set aside from revenue | |
| Earmarked Reserves | (888) |
| Revenue Financing | (12) |
| Minimum Revenue Provision (MRP) | (761) |
| Voluntary Revenue Provision (finance lease) | (246) |
| **Closing Capital Financing Requirement** | **5,301** |
| Explanation of movements in year | |
| Assets financed by prudential borrowing | 217 |
| Assets acquired under deferred purchase arrangement | 189 |
| Provision made for debt repayment | (1,007) |
| **Increase/(Decrease) in Capital Financing Requirement** | **(601)** |

The estimated CFR as at 31 March 2017 was £5.146m, so the outturn figure of £5.301m was £0.155m higher. Financing by prudential borrowing was £0.033m less than estimated when the revised CFR estimate was prepared, but expenditure on assets financed by deferred purchase was £0.171m more than estimated. MRP was £0.017m less than estimated. Overall the CFR reduced by £0.601m in 2016/17.

In this context, deferred purchase refers to the capital investment in leisure facilities being financed by means of what is known as a finance lease.

Prudential Indicator: The CFR and Borrowing

In order to ensure that local authorities only borrow for capital purposes the Prudential Code requires that borrowing, net of investments, should not exceed the CFR for the preceding year plus any anticipated increase in the current and next two years. As at 31 March 2017 net borrowing is a negative figure (see Treasury Position as at 31 March 2017 below) and is thus well below the CFR.

Compliance with Borrowing Limits

The Prudential Indicators include two borrowing limits:

• The **Operational Boundary** - This is the probable, expected limit on external debt. "Debt" consists of both borrowings and other long term liabilities (finance leases, and deferred purchase liabilities incurred under the Leisure Partnership). This was set at £0.735m and the limit has been exceeded by £0.206m. As at 31/3/17 the Council has no long-term external borrowing, and leasing liabilities stand at £0.941m.

• The **Authorised Limit** - This reflects a level of debt which the code defines as, “while not desired, could be afforded but may not be sustainable”. The limit was set at £3.735m to accommodate any planned temporary borrowings. These were not necessary and the limit set has not been breached.

Prudential Indicator: Ratio of Financing Costs to the Revenue Stream

This indicator shows what percentage of the Council’s income from Government grants and Council Tax has been used to meet interest costs and debt repayment. The indicator as per the 2016/17 Treasury Strategy forecast was 7.47%. This has fallen to an outturn of 6.74%. This is as a result of a reduction in financing costs and an increase in the net revenue stream. An increase in interest payable in respect of the leisure finance lease was offset by additional investment interest earned.

Prudential Indicator: Incremental impact of capital investment decisions

This indicator is concerned with capital expenditure over a period of years, and reports its cumulative impact on the revenue account. It is not possible to make meaningful comparison against this indicator, other than when it is restated each year when the Treasury Strategy is produced.

Treasury Position as at 31 March 2017

| | **Per Treasury Strategy 2017/18 £000** | **Actual value as at 31 March 2017 £000** |
|---|---|---|
| Total external borrowings at period end | 0 | 0 |
| Cash & investments | (31,000) | (28,687) |
| **Net External Borrowing/(Investments)** | **(31,000)** | **(28,687)** |

The forecast balance for cash and investments had taken account of the high average balance invested throughout the year, which was proved to be £35.7m for the whole financial year. However the balance as at 31 March 2017 reduced temporarily below the average. The balance as at 31 March 2017 is analysed in Appendix A.

*External and Internal Borrowing*

Please note that the Authority does use Prudential Borrowing as a source of funding its Capital Programme, and the CFR represents the total amount of borrowing incurred to finance some parts of the Capital Programme. The Authority then has a choice as to whether an actual loan is taken (from a source such as the Public Works Loan Board – PWLB) or whether it calls upon its internal cash balances instead. The decision as to whether the CFR is represented by internal or external borrowing, or a combination of the two, does not affect the calculation of the Minimum Revenue Provision.

The assessment of the lowest cost source of borrowing (internal or external) is dependent on availability of cash balances, loan interest rates available, and investment interest rates that can be secured. The annual Treasury Strategy sets out the approach for the financial year, but the position is monitored throughout the year as part of the daily Treasury Management process. All investment and borrowing decisions must be in compliance with the approved Treasury Strategy.

The Council has £5.301m of Prudential Borrowing as at 31 March 2017 but 100% of this has been funded from internal cash balances (Internal Borrowing), and therefore actual loans taken out (External Borrowing) is currently zero.

The following table summarises investments activity and returns during the year:

| Details | Average Daily Investment £'000 | Interest Earned £ | Average Rate % |
|---|---|---|---|
| Fixed Term deposits | 21,701 | 136,406 | 0.63 |
| Call accounts | 2,692 | 4,824 | 0.33 |
| Money Market Funds | 7,258 | 23,680 | 0.34 |
| Notice Accounts | 4,000 | 40,159 | 0.29 |
| Debt Management Office (DMO) | 32 | 47 | 0.15 |
| **Total** | **35,683** | **205,116** | **0.57** |

The performance benchmark is the 7-day London Inter-Bank Bid Rate (LIBID). This averaged 0.21% over the year, therefore the benchmark has been exceeded. To achieve a return rate 15% greater than LIBID (i.e. 0.24%) is a key performance indicator for Shared Financial Services, and this has been achieved.

The average rate achieved in 2015/16 was 0.55% compared to the average LIBID for that year of 0.36%. The small increase in the average rate earned in 2016/17 compared to 2015/16 reflects the full-year effect of the changes to investment counterparties approved during 2015/16. In addition, the average daily investment increased by £4.37m compared to 2015/16, which also contributed to the increase in interest earned of around £34,000.

With regard to performance against the revenue budget for Interest Earned on Investments please see the budgeted and out-turn position from 2015/16 to 2017/18:

| Actual Outturn 2015/16 £000 | Original Budget 2016/17 £000 | Estimated Outturn 2016/17 £000 | Actual Outturn 2016/17 £000 | Original Budget 2017/18 £000 |
|---|---|---|---|---|
| 171 | 165 | 188 | 205 | 69 |

The budget was exceeded in the context of a general decline in interest rates offered by investment counterparties. However, the estimated outturn was prepared at a point when the rates of interest available when maturing investments were reinvested were expected to fall. Actual interest rates offered by counterparties did not fall by as much, and the average cash balance available to invest remained high. The original budget for 2017/18 will be reviewed, and increased if considered realistic.

All investments during 2016/17 complied with the Council's policy.

Had the average daily investment been deposited with the DMO at the average rate of 0.15%, the interest earned in the year would have been only £47,000, which would have been less than a quarter of the value actually earned. The change to the list of approved counterparties in 2015/16 helped to minimise use of the DMO, because additional high credit quality counterparties offering higher returns were available as an alternative.

An analysis of the Council's cash and short-term investments as at 31 March 2017 is presented as Appendix A. The table shows the counterparties by category, and confirms that the sums invested were no greater than the appropriate limits permitted by the 2016/17 Treasury Strategy.

As in previous years, the council was unable to place deposits with a number of the larger UK financial institutions. This was usually because they were not seeking deposits from local authorities, or required larger minimum deposits than would be permitted by the Treasury Strategy. Some UK institutions did not

have sufficiently high credit quality to be used during 2016/17. Use of new counterparties permitted by changes approved during 2015/16 continued during 2016/17. These included Coventry Building Society, Goldman Sachs International, Santander UK, and German bank Helaba. No additional non-UK banks were used during 2016/17, and the impact of the decision of the UK to leave the EU will always be considered when placing investments with banks such as Helaba.

Icelandic Investment (Heritable)

There were no repayments during 2016/17 in respect of the Heritable investment claim.

Of the original £2m investment in Heritable, £1.974m has been recovered, which is around 98%. The balance of the claim against Heritable is £40,000. The Council is making every effort to recover the claim in full.

Treasury Indicator: Upper limit on exposure to variable interest rates

The authority is exposed to variable interest rates on all its invested cash. There is no real limit on such investments other than the size of the Council's cash balances. The Treasury Strategy anticipated these could peak as high as £45m. The actual peak in 2016/17 was £44.1m and therefore was below the maximum anticipated by the approved indicator. Such high balances are achieved when the Council holds council tax and business rates income prior to making payments to preceptors and central government.

**WIDER IMPLICATIONS**

In the preparation of this report, consideration has been given to the impact of its proposals in all the areas listed below, and the table shows any implications in respect of each of these. The risk assessment which has been carried out forms part of the background papers to the report.

| | |
|---|---|
| ***FINANCIAL*** | As set out in this report and its appendix |
| ***LEGAL*** | Compliance with various Regulations and Statutory Codes of Practice |
| ***RISK*** | The Council's treasury management strategy and policies are designed to ensure the effective control and management of the risks associated with such activities. |
| ***THE IMPACT ON EQUALITY*** | |
| ***OTHER (see below)*** | |

| | | | |
|---|---|---|---|
| *Asset Management* | *Corporate Plans and Policies* | *Crime and Disorder* | *Efficiency Savings/Value for Money* |
| *Equality, Diversity and Community Cohesion* | *Freedom of Information/ Data Protection* | *Health and Safety* | *Health Inequalities* |
| *Human Rights Act 1998* | *Implementing Electronic Government* | *Staffing, Training and Development* | *Sustainability* |

**BACKGROUND DOCUMENTS**

Treasury Strategy 2016/17 to 2018/19 (Council 2/3/16)
Treasury Strategy 2017/18 to 2019/20 (Council 1/3/17)

**Appendix A**

**Analysis of Cash and Investments as at 31 March 2017 (excluding accrued interest)**

| Category | Counterparty | Balance £000 | Limit per 2016/17 Treasury Strategy £000 |
|---|---|---|---|
| Call Accounts | Barclays Bank PLC | 1,114 | 4,000 |
| | Total | 1,114 | |
| Money Market Funds | Federated Sterling Liquidity Fund | 90 | 4,000 |
| | Standard Life | 450 | 4,000 |
| | Blackrock | 150 | 4,000 |
| | Total | 690 | |
| Notice Accounts | Santander (180 day notice) | 4,000 | 4,000 |
| | Total | 4,000 | |
| Term Deposits - Banks | Coventry Building Society | 3,000 | 4,000 |
| | Goldman Sachs International | 4,000 | 4,000 |
| | Bank of Scotland | 2,000 | 4,000 |
| | Nationwide Building Society | 1,000 | 4,000 |
| | Helaba ** | 3,000 | 3,000 |
| | Total | 13,000 | |
| Term Deposits - LAs | Plymouth City Council | 2,000 | 4,000 |
| | Lancashire County Council | 4,000 | 4,000 |
| | Salford City Council | 4,000 | 4,000 |
| | Total | 10,000 | |
| Total Cash and Short-Term Investments | | 28,804 | |
| Bank Overdraft net of various cash balances | | (117) | |
| Cash and Short-Term Investments net of Overdraft | | 28,687 | |

**Note**

** German bank Landesbank Hessen-Thueringen Girozentrale (known as Helaba)