REPORT FOR DECISION

MEETING:	**CABINET** **OVERVIEW & SCRUTINY COMMITTEE**
DATE:	**16 JULY 2014** **30 JULY 2014**
SUBJECT:	**2013/14 TREASURY MANAGEMENT ANNUAL REPORT**
REPORT FROM:	**LEADER OF THE COUNCIL AND CABINET MEMBER FOR FINANCE**
CONTACT OFFICER:	**STEVE KENYON, ASSISTANT DIRECTOR OF RESOURCES (FINANCE)**
TYPE OF DECISION:	**CABINET (KEY DECISION)**
FREEDOM OF INFORMATION/STATUS:	This paper is within the public domain
SUMMARY:	**PURPOSE/SUMMARY:** The Council undertakes Treasury Management Activities in accordance with the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management, which requires that the Council receives an annual strategy report by 31 March for the year ahead and an annual review report of the previous year by 30 September. This report is the review of Treasury Management activities during 2013/14.
OPTIONS & RECOMMENDED OPTION	It is recommended that, in accordance with CIPFA's Code of Practice on Treasury Management, the report be noted.
IMPLICATIONS:	
Corporate Aims/Policy Framework:	Do the proposals accord with the Policy Framework? Yes

Financial Implications and Risk Considerations:	As set out in the report and the comment of the Assistant Director of Resources (Finance and Efficiency) below.
Statement by Assistant Director of Resources (Finance and Efficiency):	This report provides information on the Council's debt, borrowing, and investment activity for the financial year ending on 31st March 2014 in conformity with the CIPFA Code of Practice for Treasury Management. The successful management of the Council's borrowing and investments is central to the Council's financial strategy, both in the short term and in ensuring a balanced debt profile over the next 25 to 60 years. The overall strategy for 2013/14 was to finance capital expenditure by running down cash/investment balances and using shorter term borrowing rather than more expensive long term loans. The taking out of longer term loans (1 to 10 years) to finance capital spending would only then be considered if required by the Council's underlying cash flow needs. Debt increased during the year, £209.943 million at 31st March 2014 compared to £203,694 million at 31st March 2013, due to the planned delayed replacement of a loan for £7.5m that matured in 2012/13 . The average borrowing rate fell from 4.43% to 3.95% due to fall out of high coupon rate debt and new short term loans. Investments at 31 March 2014 stood at £44,277 million, compared to £17,456 million the previous year, the increase being due to the receipt of grant payments towards the end of the year. The average rate of return on investments was 0.78% in 2013/14 compared to 1.67% in 2012/13.
Equality/Diversity implications:	No - (see paragraph 8.1, page 9)
Considered by Monitoring Officer:	Yes. The presentation of an annual report on Treasury Management by 30th September of the following financial year is a requirement of the Council's Financial Regulations 5.7, as part of the Council's Financial Procedure Rules and Budget and Policy framework, relating to Risk Management and Control of Resources: Treasury Management.
Are there any legal implications?	No

Staffing/ICT/Property:	There are no direct staffing, ICT or property implications arising from this report.
Wards Affected:	All
Scrutiny Interest:	Overview & Scrutiny Committee

TRACKING/PROCESS ASSISTANT DIRECTOR: STEVE KENYON

Chief Executive/ Strategic Leadership Team	Cabinet Member/Chair	Ward Members	Partners
	Yes 16/7/14		
Overview & Scrutiny Committee		Committee	Council
30/7/14			

1.0 INTRODUCTION

1.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

CIPFA defines treasury management as:

"The management of the local 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."

1.3 This report summarises the following:-

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- The actual prudential and treasury indicators;

- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity.

2.0 THE COUNCIL'S OVERALL BORROWING NEED

2.1 The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2013/14 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

2.2 Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board [PWLB] or the money markets), or utilising temporary cash resources within the Council.

2.3 The Council's (non HRA) underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision – MRP, to reduce the CFR. This is effectively a repayment of the non-Housing Revenue Account (HRA) borrowing need (there is no statutory requirement to reduce the HRA CFR). This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

2.4 The total CFR can also be reduced by:

- the application of additional capital financing resources (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

2.5 The Council's 2013/14 MRP Policy (as required by CLG Guidance) was approved as part of the Treasury Management Strategy Report for 2013/14 on 20/02/2013.

2.6 The Council's CFR for the year is shown below, and represents a key prudential indicator. It includes PFI and leasing schemes on the balance sheet, which increase the Council's borrowing need. No borrowing is actually required against these schemes as a borrowing facility is included in the contract.

Capital Financing	2012/13 Actual	2013/14 Estimate	2013/14 Actual

Requirement	£'000	£'000	£'000
CFR – non HRA	131,233	130,696	127,648
CFR – HRA existing	40,531	40,531	40,531
Housing Reform Settlement	78,253	78,253	78,253
Total CFR	**250,017**	**249,480**	**246,432**

2.7 Borrowing activity is constrained by prudential indicators for net borrowing and the CFR, and by the authorised limit. In order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2013/14) plus the estimates of any additional capital financing requirement for the current (2014/15) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2013/14. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	2012/13 Actual £'000	2013/14 Estimate £'000	2013/14 Actual £'000
Gross borrowing position	203,694	209,943	209,943
CFR	250,017	249,480	246,432

2.8 **The authorised limit** - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2013/14 the Council has maintained gross borrowing within its authorised limit.

2.9 **The operational boundary** – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

2.10 **Actual financing costs as a proportion of net revenue stream** - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2013/14 £'000
Authorised limit	288,700
Maximum gross borrowing position	220,609
Operational Boundary	253,700
Average gross borrowing position	212,113
Financing costs as a proportion of net revenue stream:-	
Non - HRA	3.21%
HRA	14.60%

3.0 TREASURY POSITION AS AT 31 March 2014

3.1 The Council's debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices. At the beginning and the end of 2013/14 the Council's treasury (excluding borrowing by PFI and finance leases) position was as follows:

	31st March 2013 Principal £'000	Average Interest Rate	31st March 2014 Principal £'000	Average Interest Rate
Fixed Rate Funding:				
- PWLB	153,862		146,362	
- Market	39,000		57,500	
- Local Bonds	3		3	
Variable Rate Funding:				
- Temporary Loans	6,000		2,000	
- PWLB	0		0	
- Market	0		0	
Bury MBC Debt	198,865		205,865	
Airport Debt	4,829		4,078	
Total Debt	**203,694**	**4.43%**	**209,943**	**3.96%**
Total Investments	**17,456**	**1.67%**	**44,277**	**0.78%**

3.2 The table below shows the maturity structure of the debt portfolio

	2012/13 Actual £'000	**2013/14 Actual £'000**
Under 12 months	14,251	8,579
12 months and within 24 months	6,059	11,280
24 months and within 5 years	12,352	19,078
5 years and within 10 years	14,026	14,000
10 years and within 15 years	550	550
15 years and over	156,456	156,456
Total Debt	**203,694**	**209,943**

3.3 All the investments held are for a period of less than one year.

4.0 OVERVIEW OF THE STRATEGY FOR 2013/14

4.1 The strategy for 2013/14 was to finance capital expenditure by running down cash/investment balances and use short term loans at lower rates of interest than more expensive long term loans. These loans would be postponed as long as it is prudent to do so. One PWLB loan of £7.5m was repaid in the year together with an Airport loan of £0.279m. In line with the strategy, these loans, together with a PWLB loan of £7.5m repaid in 2012/13 which was not replaced in the year, have been replaced by shorter term 2-3 year market loans, at lower interest rates. All other borrowing in the year comprised temporary short term loans.

4.2 As a result of 3.1 above, the Council was able to lower the average interest rate on debt from 4.43% to 3.96%. Due to poor investment returns, the average interest rate on investments fell to 0.78% in 2013/14 compared to an average rate of 1.67% for 2012/13.

4.3 Grants received towards the end of the financial year meant a temporary increase in investment balances at 31st March 2014.

5.0 ECONOMIC REVIEW FOR 2013/14

5.1 The original expectation for 2013/14 was that Bank Rate would not rise during the year and for it only to start gently rising from quarter 1 2015. This forecast rise has now been pushed back to a start in quarter 3 2015. Economic growth (GDP) in the UK was virtually flat during 2012/13 but showed signs of improvement during the year. Consequently there was no additional quantitative easing during 2013/14 and 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 also expected to remain slightly below the target rate for most of the two years ahead.

5.2 Gilt yields were on a sharply rising trend during 2013 but volatility returned in the first quarter of 2014 as various fears sparked a flight to quality. The Funding for Lending Scheme, announced in July 2012, resulted in a flood of cheap credit being made available to banks which then resulted in money market investment rates falling drastically in the second half of that year and continuing into 2013/14. That part of the Scheme which supported the provision of credit for mortgages was terminated in the first quarter of 2014 as concerns rose over resurging house prices.

5.3 The UK coalition Government maintained its tight fiscal policy stance and recent forecasts indicate a reduction in the forecasts for total borrowing over the next five years.

5.4 The EU sovereign debt crisis subsided during the year as confidence in the ability of the Eurozone remained intact. Perceptions of counterparty risk improved after the ECB statement in July 2012 that it would do "whatever it takes" to support struggling Eurozone countries; this led to a return of confidence in its banking system which has continued into 2013/14 and led to a move away from only very short term investing. However, this is not to say that the problems of the Eurozone, or its banks, have ended as the zone 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. Upcoming stress tests of Eurozone banks could also reveal some areas of concern.

6.0 BORROWING OUTTURN FOR 2013/14

6.1 The Council's ability to borrow is determined by the cumulative capital financing requirement (CFR). When the cumulative CFR is compared to outstanding debt the difference is the amount of headroom still available to borrow. At the end of 2013/14 debt stood at £209.943m and the CFR at £246.432m. Therefore, in theory, borrowing of £36.489m could be taken to finance past and present capital expenditure.

6.2 An analysis of movements at nominal values on loans during the year is shown below:

	Balance at 31/03/13	Loans raised	Loans repaid	Balance at 31/03/14
	£000's	£000's	£000's	£000's
PWLB	153,862	0	(7,500)	146,362
Market	39,000	18,500	0	57,500
Temporary Loans	6,000	2,000	(6,000)	2,000
Other loans	3	0	0	3
Bury MBC Debt	**198,865**	**20,500**	**(13,500)**	**205,865**
Airport PWLB Debt	4,829	0	(751)	4,078
Total Debt	**203,694**	**20,500**	**(14,251)**	**209,943**

6.3 The loans raised during the year are shown below. Additional loans were taken out during the year to replace a PWLB loan, for £7.5m, that matured but which was not replaced in 2012/13.

Lender	Rate	Amount £000's	Start Date	End Date
County Council	1.13%	5,000	05/04/2013	05/07/2016
Fire Authority	0.39%	2,000	15/07/2013	14/07/2014
Police Authority	0.68%	2,000	08/08/2013	24/07/2016
County Council / Fire & Rescue Authority	1.06%	5,500	15/10/2013	22/04/2016
County Council / Police & Crime Commissioner	1.06%	4,000	21/10/2013	21/04/2016
County Council	1.06%	2,000	01/11/2013	22/04/2016
Total		**20,500**		

6.4 The approach during 2013/14 was to take advantage of rates when they were at their lowest and identify debt rescheduling opportunities. Unfortunately, there were no opportunities to make savings through debt rescheduling in 2013/14.

6.5 In line with the strategy, the Council delayed borrowing as long as possible by running down short term investments. When it was time to borrow, shorter term loans were taken in preference to more expensive long term loans. By maintaining borrowing at short term rates, the Council was able to minimise any corresponding risk from holding short term investments. As the year progressed further borrowing was kept to a minimum and cash balances were used to finance new capital expenditure. Therefore counterparty risk incurred on investments was minimised. This also maximised treasury management budget savings as investment rates were much lower than most new borrowing rates.

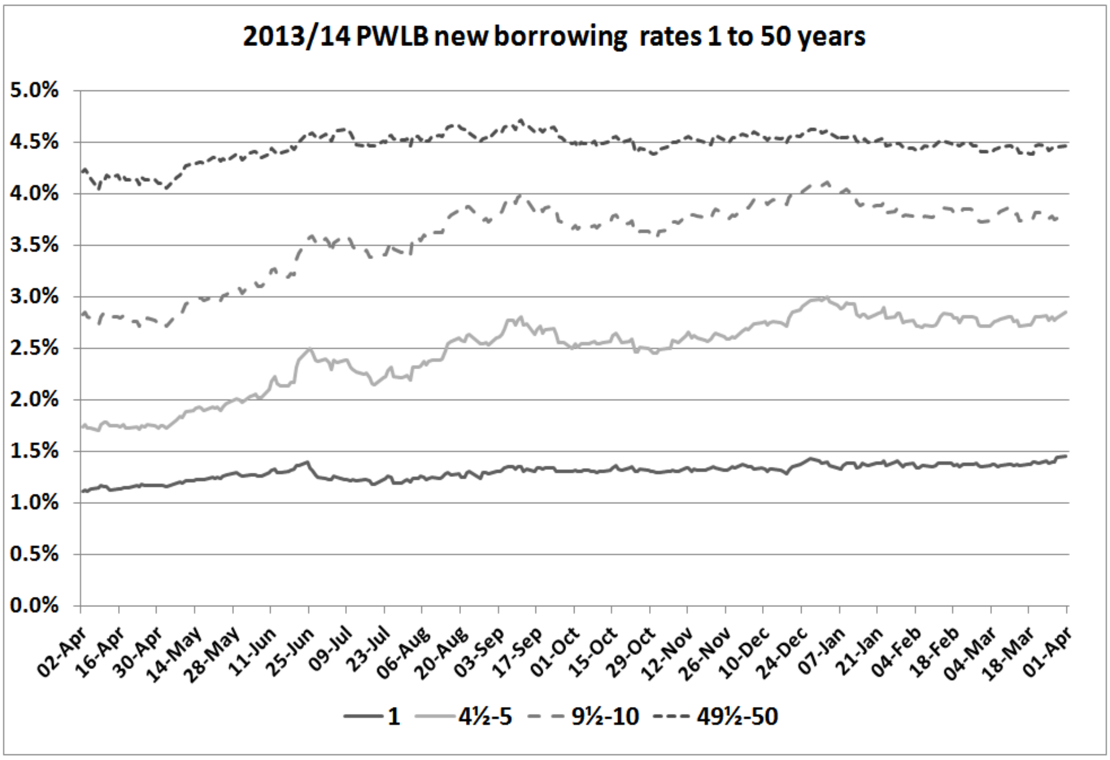
6.6 The active monitoring of the debt portfolio, the full year effect of previous rescheduling of loans, and the taking of new loans at historically low rates, have decreased the average Interest rate on the debt held over time:

Year	07/08	08/09	09/10	10/11	11/12	12/13	13/14
Average Interest Rate on Debt	5.40%	5.33%	4.98%	4.81%	4.56%	4.43%	3.96%

6.7 From 2007/08 the average interest rate falls over time due to rescheduling of loans to lower interest rates and the borrowing of new loans at historically low levels.

6.8 The Council's policy on the fall out of debt has been to establish a debt profile where the amount of debt due to be refinanced each year is stable and large scale financing in any one year avoided. Market LOBO (Lenders Option Borrower's Option) loans are recorded in accordance with the regulations set down in the Prudential Code which states "the maturity of borrowing should be determined by reference to the earliest date on which the lender can require payment".

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



7.0 INVESTMENT OUTTURN FOR 2013/14

7.1 The Council's investment policy is governed by CLG guidance, which was been implemented in the annual investment strategy approved by the Council on 20 February 2013. This policy set 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 (such as rating outlooks, credit default swaps, bank share prices etc.).

7.2 The Council manages its investments in-house (with advice from Capita Asset Services) with the overall objective to balance risk with return and the overriding consideration being given to the security of the available funds.

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

7.4 The strategy recognised that the Council's funds would be mainly cash-flow driven. The Council would seek to utilise business reserve accounts and short dated deposits in order to benefit from the compounding of interest.

7.5 Detailed below is the result of the investment strategy undertaken by the Council.

	Average Investment	Rate of Return	Benchmark Return *
Internally Managed	£54,517,602	0.78%	0.35%

* the benchmark return is the average 7-day London Interbank Bid (LIBID) rate sourced from Capita Asset Services

7.6 Investments at 31 March 2014 stood at £44.277m (£17.456m at 31 March 2013), whilst the average for the year was £54.517m (£35.416m at 31 March 2013).

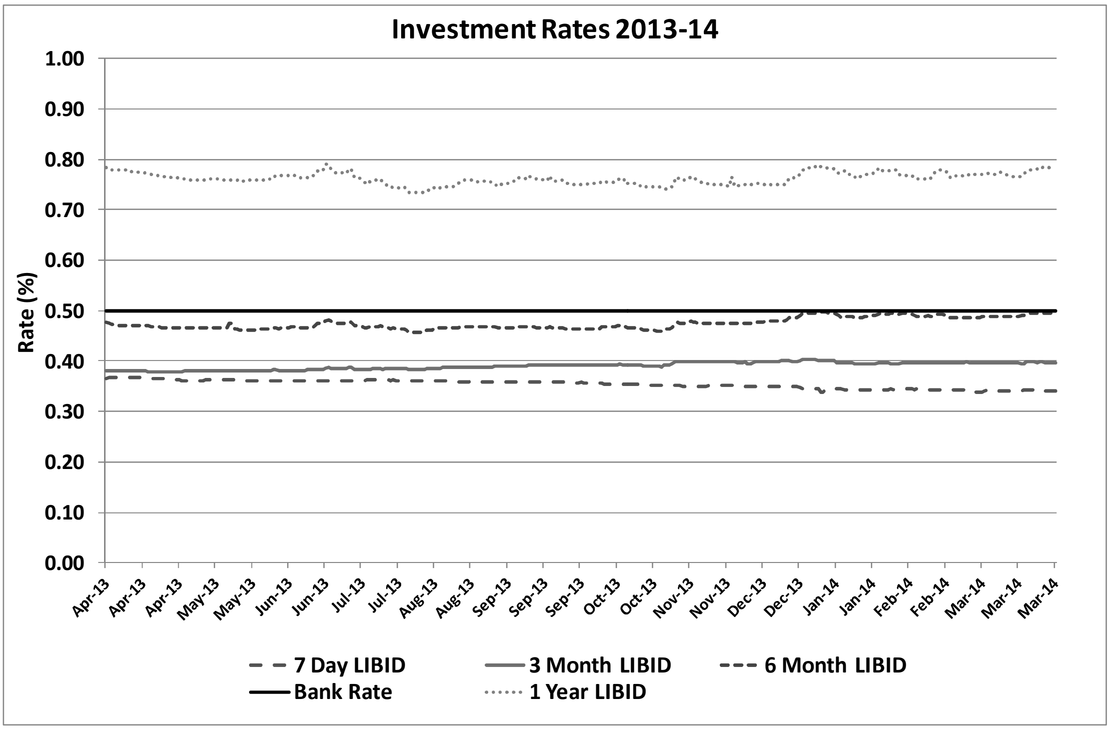
	Investment at 31/03/13 £000's	Amount Invested in year £000's	Investments realised in year £000's	Balance at 31/03/14 £000's
Fixed Rate Investments				
Royal Bank of Scotland	3,700	0	(3,700)	0
Bank of Scotland	9,600	19,600	(9,600)	19,600
District Council	0	6,200	(6,200)	0
County Council	0	1,200	0	1,200
Total - Fixed rate	**13,300**	**27,000**	**(19,500)**	**20,800**
Call Accounts				
Bank of Scotland - Call Account	0	224,690	(224,690)	0
NATWEST bank - Call Account	4,156	55,521	(36,200)	23,477
Total Investments	**17,456**	**307,211**	**(280,390)**	**44,277**

7.7 The table below gives details of the fixed rate investments made during the year.

	Rate	Amount £000's	Start Date	End Date
Bank of Scotland	1.10%	5,000	11/04/2013	10/04/2014
Bank of Scotland	1.01%	2,500	18/07/2013	17/07/2014
Bank of Scotland	0.98%	2,100	10/10/2013	09/10/2014
District Council	0.43%	6,200	10/12/2013	28/02/2014
Bank of Scotland	0.95%	5,000	28/02/2014	27/02/2015
County Council	0.60%	1,200	28/02/2014	27/02/2015
Bank of Scotland	0.95%	5,000	20/03/2014	19/03/2015
Total		**27,000**		

7.8 Total interest earned on investments in the financial year was £0.418 million compared to £0.589 million in 2012/13. This reflects the fact that investment returns were poor throughout the year.

7.9 The Bank Rate remained at it's historic low of 0.5% throughout the year; it has now remained unchanged for five years. Market expectations as to the timing of the start of monetary tightening ended up almost unchanged at around the end of 2014 / start of 2015. The Funding for Lending Scheme resulted in deposit rates remaining depressed during the whole of the year, although the part of the scheme supporting provision of credit for mortgages came to an end in the first quarter of 2014.



8.0 COMPLIANCE WITH TREASURY LIMITS

8.1 During the financial year the Council operated within the treasury limits and Prudential Indicators set out the Council's Treasury Policy Statement and annual Treasury Management Strategy Statement. The outturn for the Prudential Indicators is shown in Appendix 1.

9.0 EQUALITY AND DIVERSITY

9.1 There are no specific equality and diversity implications.

10.0 FUTURE ACTIONS

10.1 Treasury Management Updates and Prudential Indicators for 2014/15 will be presented on a quarterly basis to the Cabinet and the Overview & Scrutiny Committee.

11.0 CONCLUSION

11.1 It is recommended that Members note the treasury management activity that has taken place during the financial year 2013/14.

Councillor Mike Connolly
Leader of the Council and Cabinet Member for Finance

Background documents:

Unaudited Final Accounts Bury MBC 2013/14
CIPFA Treasury Management Code of Practice in the Public Services
CIPFA The Prudential Code for Capital Finance in Local Authorities
Capita Asset Management Treasury Management Report 2013-14
Financial markets and economic briefing papers
For further information on the details of this report and copies of the detailed variation sheets, please contact:

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