REPORT FOR DECISION

Bury COUNCIL

MEETING:	**COUNCIL** **CABINET** **OVERVIEW & SCRUTINY COMMITTEE**
DATE:	**9 SEPTEMBER 2015** **8 JULY 2015** **29 JULY 2015**
SUBJECT:	**2014/2015 TREASURY MANAGEMENT ANNUAL REPORT**
REPORT FROM:	**DEPUTY LEADER OF THE COUNCIL AND CABINET MEMBER FOR FINANCE AND HOUSING**
CONTACT OFFICER:	**Steve Kenyon, Interim Executive Director of Resources and Regulation**

TYPE OF DECISION:	**CABINET KEY DECISION**
FREEDOM OF INFORMATION/STATUS:	This paper is within the public domain

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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 2014/15.

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	As set out in the report and the comment of

Considerations:	the Interim Executive Director of Resources and Regulation 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 2015 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 2014/15 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 decreased during the year, £201.364 million at 31st March 2015 compared to £209,943 million at 31st March 2014. The average borrowing rate fell from 3.95% to 3.93% due to fall out of high coupon rate debt and new short term loans. Investments at 31 March 2015 stood at £32,332 million, compared to £44,277 million the previous year, the decrease being due to the use of cash/investment balances to repay maturing debt. The average rate of return on investments was 0.62% in 2014/15 compared to 0.78% in 2013/14.
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 **INTERIM EXECUTIVE DIRECTOR: STEVE KENYON**

Chief Executive/ Strategic Leadership Team	Cabinet	Ward Members	Partners
22/05/15	08/7/15		
Overview & Scrutiny Committee		Committee	Council
29/7/15			**9/9/15**

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 2014/15 unfinanced capital expenditure, 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 MRP Policy (as required by CLG Guidance) was approved as part of the Treasury Management Strategy Report for 2014/15 on 19/02/2014.

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 Requirement	**2013/14 Actual £'000**	**2014/15 Estimate £'000**	**2014/15 Actual £'000**
CFR – non HRA	127,648	130,949	122,029
CFR – HRA existing	40,531	40,531	40,531
Housing Reform Settlement	78,253	78,253	78,253
Total CFR	**246,432**	**249,733**	**240,813**

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 (2014/15) plus the estimates of any additional capital financing requirement for the current (2015/16) 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 2014/15. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	2013/14 Actual £'000	2014/15 Estimate £'000	2014/15 Actual £'000
Gross borrowing position	209,943	201,364	201,364
CFR	246,432	249,733	240,813

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 2014/15 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.

	2014/15 £'000
Authorised limit	283,700
Operational Boundary	248,700
CFR	240,813
Gross borrowing position	201,364

3.0 TREASURY POSITION AS AT 31 March 2015

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 2014/15 the Council's treasury (excluding borrowing by PFI and finance leases) position was as follows:

		31st March 2014			31st March 2015		
		Principal		Avg.	Principal		Avg.
		£0	£0	Rate	£0	£0	Rate
Fixed rate funding							
	PWLB Bury	146,362			140,553		
	PWLB Airport	4,078			3,308		
	Market Bury	57,500	207,940		57,500	201,361	
Variable rate funding							
	PWLB Bury	0			0		
	Market Bury	0	0		0	0	
Temporary Loans / Bonds		2,003	2003		3	3	
Total Debt			**209,943**	**3.96%**		**201,364**	**3.93%**
Total Investments			**44,277**	**0.78%**		**32,322**	**0.62%**

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

	2013/14 Actual £'000	2014/15 Actual £'000
Under 12 months	8,579	11,853
12 months and within 24 months	11,280	16,806
24 months and within 5 years	19,078	11,698
5 years and within 10 years	14,000	4,000
10 years and within 15 years	550	550
15 years and over	156,456	156,456
Total Debt	**209,943**	**201,364**

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

4.0 OVERVIEW OF THE STRATEGY FOR 2014/15

4.1 The strategy for 2014/15 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. Two PWLB loans totalling £5.8m were repaid in the year together with an Airport loan of £0.25m. In line with the strategy, these loans repayments were financed by cash or investment balances rather than replacement loans.

4.2 As a result of 3.1 above, the Council was able to lower the average interest rate on debt from 3.96% to 3.93%. Due to poor investment returns, the average interest rate on investments fell to 0.62% in 2014/15 compared to an average rate of 0.78% for 2013/14. The Council is seeking to redress this through its Property Investment Strategy

5.0 ECONOMIC REVIEW FOR 2013/14

5.1 The original market expectation at the beginning of 2014/15 was for the first increase in Bank Rate to occur in quarter 1 2015 as the unemployment rate had fallen through the Bank of England's initial forward guidance target of 7%. In May, however, the Bank revised its forward guidance. A combination of very weak pay rises and inflation above the rate of pay rises meant that consumer disposable income was still being eroded and in August the Bank halved its forecast for pay inflation in 2014 from 2.5% to 1.25%. Expectations for the first increase in Bank Rate therefore started to recede as growth was still heavily dependent on consumer demand. During the second half of 2014 financial markets were caught out by a halving of the oil price and the collapse of the peg between the Swiss franc and the euro. Fears also increased considerably that the ECB was going to do too little too late to ward off the threat of deflation and recession in the Eurozone. By the end of 2014, it was clear that inflation in the UK was going to head towards zero in 2015 and possibly even turn negative. In turn, this made it clear that the MPC would have great difficulty in starting to raise Bank Rate in 2015 while inflation was around zero and so market expectations for the first increase receded back to around quarter 3 of 2016.

5.2 Gilt yields were on a falling trend for much of the last eight months of 2014/15 but were then pulled in different directions by increasing fears after the anti-austerity parties won power in Greece in January; developments since then have increased fears that Greece could be heading for an exit from the euro. While the direct effects of this would be manageable by the EU and ECB, it is very hard to quantify quite what the potential knock on effects would be on other countries in the Eurozone once the so called impossibility of a country leaving the EZ had been disproved. Another downward pressure on gilt yields was the announcement in January that the ECB would start a major programme of quantitative easing, purchasing EZ government and other debt in March. On the other hand, strong growth in the US caused an increase in confidence that the US was recovering from the financial crash and would be the first country to start increasing its central rate, probably by the end of 2015. The UK would be closely following it due to growth over both 2013 and 2014 and prospects for a continuation into 2015 and beyond. However, there was also an increase in concerns around political risk from the general election due in May 2015.

5.3 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 throughout 2014/15.

5.4 The UK coalition Government maintained its tight fiscal policy stance but recent economic growth and gilt yields led to a reduction in the forecasts for total borrowing in the March budget.

5.5 The EU sovereign debt crisis The EU sovereign debt crisis had subsided since 2012 until the Greek election in January 2015 sparked a resurgence of fears. While the UK and its banking system has little direct exposure to Greece, it is much more difficult to quantify quite what effects there would be if contagion from a Greek exit from the euro were to severely impact other major countries in the EZ and cause major damage to their banks.

6.0 BORROWING OUTTURN FOR 2014/15

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 2014/15 debt stood at £201,364m and the CFR at £240,813m. Therefore, in theory, borrowing of £39,499m 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 31/03/14 £000's	Loans raised £000's	Loans repaid £000's	Balance at 31/03/15 £000's
PWLB	146,362	0	(5,809)	140,553
Market	57,500	0	0	57,500
Temporary Loans	2,000	3,000	(5,000)	0
Other loans	3	0	0	3
Bury MBC Debt	**205,865**	**3,000**	**(10,809)**	**198,056**
Airport PWLB Debt	4,078	0	(770)	3,308
Total Debt	**209,943**	**3,000**	**(11,579)**	**201,364**

6.3 Due to low investment returns, no borrowing was undertaken during the year.

6.4 No debt rescheduling was undertaking during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

6.5 In line with the strategy, the Council reduced borrowing by running down short term investments 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.

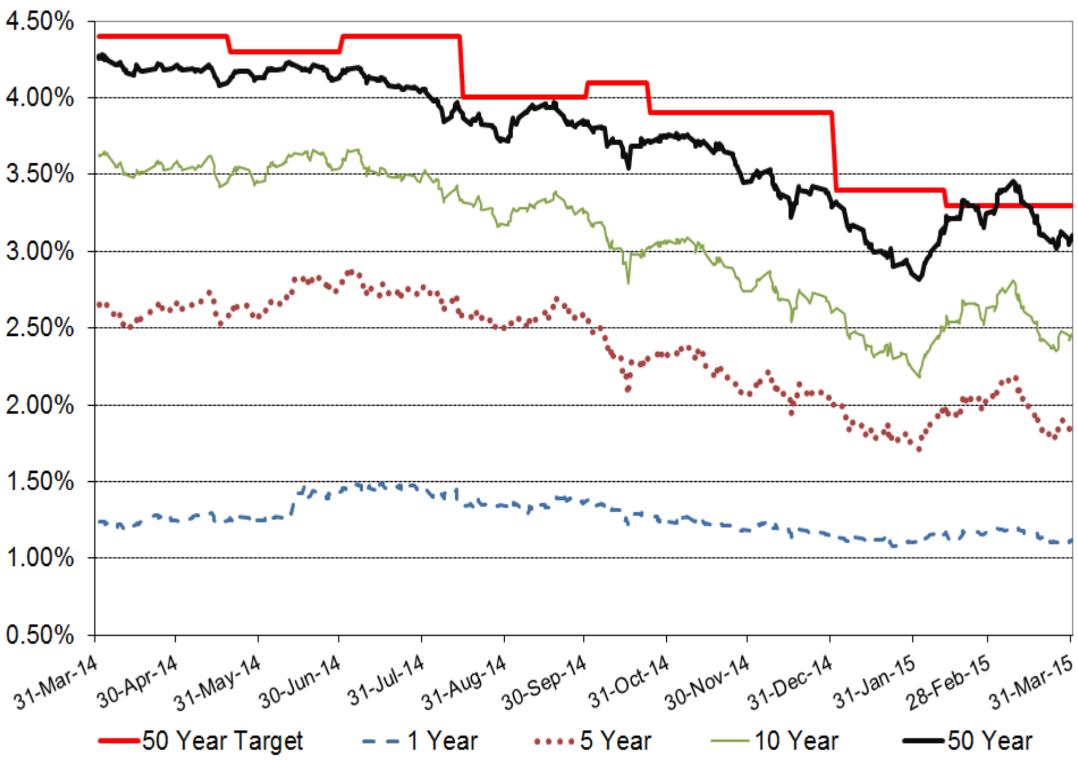
6.6 The active monitoring of the debt portfolio, the full year effect of previous rescheduling of loans, and the taking of new loans at historically low rates, have decreased the average Interest rate on the debt held over time:

Year	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
Average Interest Rate on Debt	5.33%	4.98%	4.81%	4.56%	4.43%	3.96%	3.96%

6.7 From 2008/09 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 certainty maturity 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 2014/15

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 19 February 2014. 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	£62,687,589	0.62%	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 2015 stood at £32.322 (£44.277m at 31 March 2014).

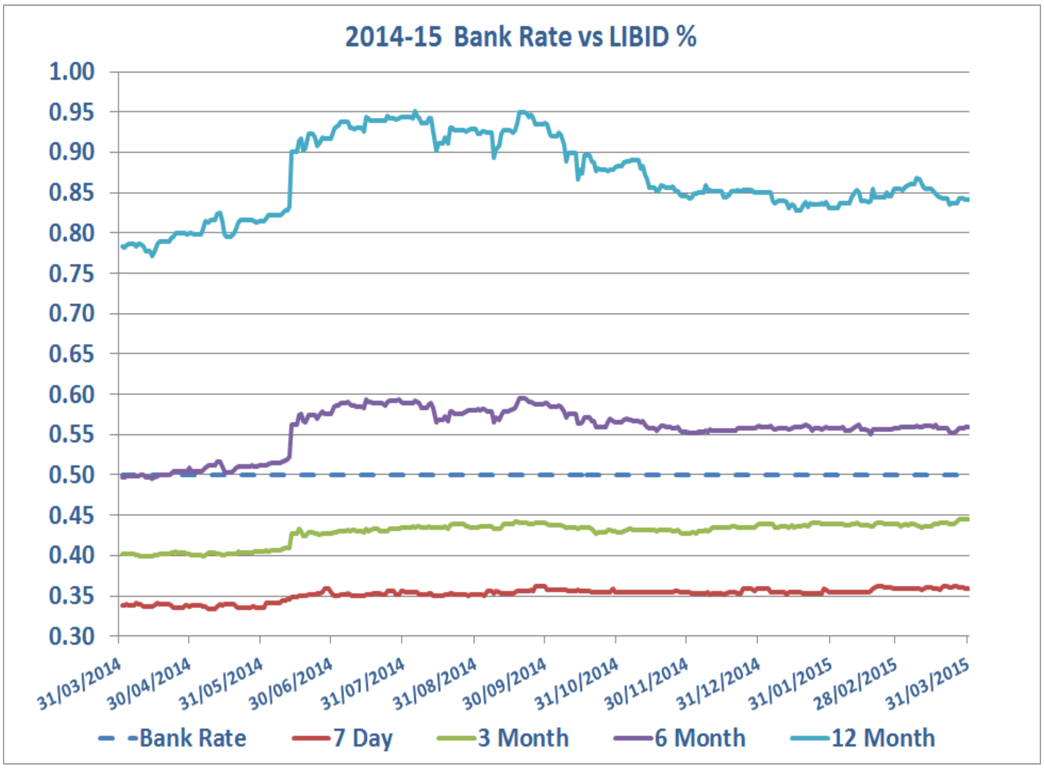
	Investment at 31/03/14 £000's	**Amount Invested in year £000's**	**Investments realised in year £000's**	**Balance at 31/03/15 £000's**
Fixed Rate Investments				
Nationwide Building Society	0	32,000	(22,000)	10,000
Bank of Scotland	19,600	14,000	(19,600)	14,000
Coventry Building Society	0	22,000	(22,000)	0
Barclays Bank	0	16,000	(10,000)	6,000
Lancashire CC	1,200	0	(1,200)	0
Total - Fixed rate	**20,800**	**84,000**	**(74,800)**	**30,000**
Call Accounts				
Barclays Bank - Flexible Interest Bearing Current Account	0	15,037	(14,115)	922
Bank of Scotland - Call Account	0	184,050	(182,650)	1,400
NATWEST bank - Call Account	23,477	93,750	(117,227)	0
Total Investments	**44,277**	**376,837**	**(388,792)**	**32,322**

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	0.95%	5,000	10/04/2014	01/04/2015
Nationwide	0.47%	2,000	17/04/2014	17/07/2014
Nationwide	0.49%	8,000	12/05/2014	12/08/2014
Coventry Building Society	0.45%	5,300	03/07/2014	03/10/2014
Coventry Building Society	0.45%	4,700	07/07/2014	07/10/2014
Nationwide	0.54%	2,000	17/07/2014	17/11/2014
Barclays	0.59%	8,000	06/08/2014	06/01/2015
Nationwide	0.54%	8,000	12/08/2014	12/12/2014
Barclays	0.48%	1,000	15/08/2014	17/11/2014
Coventry Building Society	0.45%	5,000	03/10/2014	05/01/2015
Coventry Building Society	0.45%	3,000	07/10/2014	07/01/2015
Bank of Scotland	1.00%	2,000	17/11/2014	01/04/2015
Barclays	0.51%	1,000	17/11/2014	16/02/2015
Nationwide	0.66%	8,000	12/12/2014	01/04/2015
Barclays	0.61%	5,000	06/01/2015	01/04/2015
Nationwide	0.46%	2,000	06/01/2015	06/03/2015
Coventry Building Society	0.43%	4,000	07/01/2015	09/03/2015
Barclays	0.48%	1,000	16/02/2015	01/04/2015
Bank of Scotland	1.00%	5,000	27/02/2015	01/04/2015
Nationwide	0.46%	2,000	06/03/2015	01/04/2015
Bank of Scotland	1.00%	2,000	19/03/2015	01/04/2015
Total		**84,000**		

7.8 Total interest earned on investments in the financial year was £0.379 million compared to £0.418 million in 2013/14. This reflects the fact that investment returns were poor throughout the year. The Council is seeking to redress this through it's Property Investment Strategy.

7.9 The Bank Rate remained at it's historic low of 0.5% throughout the year; it has now remained unchanged for six years. Market expectations as to the timing of the start of monetary tightening started the year at quarter 1 2015 but then moved back to around quarter 3 2016 by the end of the year. Deposit rates remained depressed during the whole of the year, primarily due to the effects of the Funding for Lending Scheme.



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.

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 2015/16 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 2014/15.

Councillor Rishi Shori
Deputy Leader of the Council and Cabinet Member for Finance and Housing

Background documents:

Unaudited Final Accounts Bury MBC 2014/15
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 2014-15
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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