Part I
Item No: 8(c)
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All Wards

WELWYN HATFIELD BOROUGH COUNCIL
CABINET – 12 JULY 2016
REPORT OF THE DIRECTOR (FINANCE AND OPERATIONS)

TREASURY MANAGEMENT ANNUAL REPORT 2015/16

1 Executive Summary

1.1 In February 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, and also receive mid and end of year reports. This report therefore reviews the treasury management activity and prudential indicators for the 2015/16 financial year.

2 Recommendation

2.1 It is recommended that Cabinet note the report and actual treasury management prudential indicators for 2015/16.

3 Background

3.1 The Council approved the 2015/16 Treasury Management Strategy at its meeting on 1 February 2015.

3.2 Treasury management is defined 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." The main aim of the investment strategy then was to ensure the security of funds, maintain liquidity and within those parameters, achieve the best possible return.

3.3 The Director (Finance and Operations) is pleased to report that all treasury management activity undertaken during the financial year complied with the approved strategy, the CIPFA Code of Practice, and the relevant legislative provisions.

4 Economic review

4.1 The Council's treasury consultants, Arlingclose Ltd have provided an economic review of the year, which is attached at Appendix A.

4.2 For Members' information, following the results of the EU referendum, Arlingclose have not changed their current investment advice but will be monitoring economic and market activity closely, keeping clients fully informed. They have highlighted their clients already focus investment activity on low risk institutions, such as the highest quality banks and building societies. In addition, their credit advice has been positioned for some time with uncertainty in mind, with current advised durations shorter than those outlined in their template Treasury Management Strategy.

4.3 They believe the Government and the Bank of England have both the tools and the willingness to use them to prevent any immediate market-wide problems leading to bank insolvencies. Their cautious approach to credit advice means that the banks currently on our counterparty list have sufficient equity buffers to deal with any localised problems in the short term. Mark Carney's statement on 24 June reaffirmed these points. There is therefore no immediate change to their credit advice on UK banks and building societies, nor for any other institutions. There is a risk that the vote to leave the EU, and the consequent uncertainty over UK future trading prospects, will bring forward the timing of the next UK recession. In the coming weeks and months they will therefore review all UK based institutions, and it is likely that, over time, they will shorten their advised durations on those they consider to be most affected.

5 Borrowing and investment portfolio

Borrowing

5.1 A summary of investments and borrowing as at 31 March 2016 is attached at Appendix B.

5.2 No new external borrowing was entered into during 2015/16 so the table below shows the movement in year relating to the HRA self funding debt. Total interest paid in the year amounted to £6.574m.

HRA loans	Balance on 01/04/2015 £'000	Matured in 2015/16 £'000	Balance on 31/03/2016 £'000	Average rate** on.31/03/16 %
Short term loans*	11,750	11,750	13,500	1.22
Long term loans	265,399	0	251,899	2.53
Total	277,149	11,750	265,399	2.45

*Loans with maturities within 1 year **Not time weighted

Investments

5.3 The average investment balance during 2015/16 was £70.48m.The tables below summarise the investment activity, weighted average investment rates and total interest earned during 2015/16.

Investment Counterparty	Balance on 31/03/2015 £'000	Investments Made £'000	Maturities/ Investments Sold £'000	Balance on 31/03/2016 £'000
UK Central Government - Short term	0	20,966	20,966	0
UK Local Authorities - Short term - Long term	0 4,000	2,000 0	0 0	2,000 4,000
Banks & Building Societies - ST deposits/accounts - ST negotiable - ST negotiable (secured) - LT fixed deposits	 30,408 3,000 0 0	 78,681 16,073 7,052 1,000	 88,356 10,068 7,052 0	 20,733 9,005 0 1,000

- LT negotiable - LT negotiable (secured)	2,060 1,000	0 3,170	2,060 92	0 4,078
AAA rated Money Market Funds	17,611	154,315	160,926	11,000
Pooled Property Fund	0	4,000	0	*4,000
Corporates - ST negotiable	2,006	11,957	13,892	71
Registered Providers - Long term	185	0	0	185
TOTAL INVESTMENTS	**60,270**	**299,214**	**303,412**	**56,072**

*Net Asset Value of shares at 31/03/16 = £3.799m

Short term & pooled investments	0.62%
Long term investments	2.19%
All investments	0.83%
Total interest earned	£569,000

5.4 The maturity profile of all investments at and from 31 March 2016 is shown below:

	£'000
Up to 1 month	20,644
1-3 months	9,093
3-6 months	12,000
6 months-1 year	4,149
1-3 years	3,001
3-5 years	*4,185
Total	56,072

*Property Fund investment period anticipated to be at least 3-5 years

5.5 In 2015, the transposition of two European Union directives into UK legislation placed the burden of rescuing failing EU banks disproportionately onto unsecured institutional investors, which include local authorities and pension funds. During the year, all three credit ratings agencies therefore reviewed their ratings to reflect the loss of government support for most financial institutions and the potential for loss given default as a result of these new 'bail-in' regimes in many countries. Despite reductions in government support many institutions saw upgrades due to an improvement in their underlying strength and an assessment that that the level of loss given default is low.

5.6 At the end of July 2015, Arlingclose advised an extension of recommended durations for unsecured investments in certain UK and European institutions following improvements in the global economic situation and the receding threat of another Eurozone crisis. A similar extension was advised for some non-European banks in September, and certain non-rated UK building societies also being extended. In January 2016, Arlingclose also supplemented its existing investment advice with a counterparty list of high quality bond issuers, including recommended cash and duration limits

5.7 This action allowed some slightly longer short term investments to be made and the continued use of negotiable instruments such as bonds and certificates of deposits. Opportunities to invest in secured short and long term bonds were also taken, due to their exemption from bail in.

5.8 A decision was also made to invest in a pooled property fund, currently yielding over 4% per annum, which allows diversification into an asset class other than cash without the need to own and manage the underlying investments. The fund is operated on a variable net asset value (VNAV) basis which offers diversification of investment risk coupled with the services of a professional fund manager. It offers enhanced returns over the longer term but is more volatile in the short term. Although money can be redeemed from the fund with notice, it is the intention to hold the shares for at least 3-5 years. Its performance and suitability in meeting investment objectives will therefore be monitored regularly and discussed with Arlingclose.

6 Treasury Management indicators

6.1 The actual treasury management indicators for the 2015/16 financial year were as follows:-

6.2 Interest rate exposures

This indicator is set to control the Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest exposures, expressed as an amount of net principal borrowed were:

	Limit	Maximum in 14/15	Limit observed in year
Upper limit on fixed interest rate exposures	£300m	£259.2m	✓
Upper limit on variable interest rate exposures	£0m	-£29.1m	✓

6.3 Maturity structure of borrowing

This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing were:

	Upper Limit	Lower Limit	Actual at 31.3.16	Limit observed in year
Under 12 months	10%	0%	5.1%	✓
12 months and within 24 months	15%	0%	5.8%	✓
24 months and within 5 years	30%	0%	21.0%	✓
5 years and within 10 years	60%	0%	45.8%	✓
10 years and within 20 years	100%	0%	22.3%	✓

Time periods for this indicator start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

6.4 Principal sums invested for periods longer than 364 days

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits were:

	2015/16 £'000	2016/17 £'000	2017/18 £'000
Limit on principal invested beyond year end as at 31/03/16	20,000	17,000	15,000
Actual principal invested beyond year end As at 31/03/16	13,263	10,186	10,186
Limit observed in year	✓	✓	✓

7 Future treasury activity

7.1 It is to be noted that proposals relating to the authority's Affordable Housing Programme and the prospective establishment of a Property Company will have some effect on treasury management activity in forthcoming years. Members will therefore receive further details as and when appropriate on these matters.

Implications

8 Legal Implications

8.1 This report contains no legal implications.

9 Financial Implications

9.1 This report is for information only so has no direct financial implications.

10 Risk Management Implications

10.1 Management of risk associated with investment and borrowing is the main objective of the Council's treasury management strategy. This is achieved through robust counterparty monitoring and selection criteria, prudent cash flow forecasting, a range of exposure limits and indicators, and procedures designed to prevent fraud and error.

11 Security & Terrorism Implications

11.1 This report contains no security or terrorism implications.

12 Procurement Implications

12.1 This report contains no procurement implications.

13 Climate Change Implications

13.1 This report contains no climate change implications.

14 Link to Corporate Priorities

14.1 The subject of this report is linked to the Council's Corporate Priority 'Engage with our communities and provide value for money' and specifically to the achievement of 'Deliver value for money'.

15 Equality and Diversity

15.1 An Equality Impact Assessment (EIA) has not been carried out in connection with the proposals that are set out in this report.

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Appendix A – Arlingclose Ltd – Economic Context
Appendix B – Investments and Loans at 31 March 2016