

This report ensures the council demonstrates best practice in accordance with CIPFA's recommendations in their Code of Practice for Treasury Management, by keeping Members informed of treasury management activity.

1. The Economy

1.1. Recent economic events and statistics show the following:

- The UK economic recovery has continued and now appears more sustainable. GDP for the first quarter of 2014 showed the UK economy growing by 0.8% over the quarter and 3.0% year-on-year
- The year-on-year Consumer Price Index (CPI) fell to 1.5% in May.
- The unemployment rate fell to 6.6% in the three months to April. However, earnings growth has weakened with total pay slowing to just 0.7% yearly growth in the same period.
- There has been no change in the Bank Base Rate. However, there has recently been a marked shift in tone from the Bank of England's Governor and other Monetary Policy Committee (MPC) members warning that interest rates might rise sooner than financial markets are expecting. Continuing positive economic momentum in the second half of 2014 may mean that some MPC members will start to vote for a rise sooner rather than later.
- With slack in the labour markets, low inflation and weak earnings growth, the council's treasury advisers, Arlingclose, forecast the first increase to be late 2015 at the earliest.

2. The Council's Investments

2.1 At 30th June 2014 the council held the following investments:

Investment	Term	Maturity Date	Interest Rate	Amount invested	
				£m	£m
<u>Instant Access Bank Accounts:</u>					
National Westminster	N/A	N/A	0.25%	0.05	
Handelsbanken	N/A	N/A	0.60%	5.00	5.05
<u>Instant Access Money Market Funds:</u>					
Ignis	N/A	N/A	0.44%	5.00	
Prime Rate	N/A	N/A	0.41%	2.82	7.82
<u>1 Month Notice Account</u>					
Close Bros	N/A	N/A	1.00%	5.00	5.00
<u>Fixed Term Deposits:</u>					
Lloyds	182 days	25/07/14	0.75%	1.50	
Lloyds	181 days	19/08/14	0.70%	2.00	
Nationwide	298 days	23/01/15	0.72%	2.00	
Barclays	365 days	19/02/15	0.85%	1.00	
Nationwide	279 days	25/03/15	0.79%	2.00	
Barclays	279 days	25/03/15	0.79%	1.00	
Lloyds	364 days	27/03/15	0.95%	1.00	
Barclays	364 days	27/03/15	0.86%	1.00	
Bank of Scotland	364 days	30/03/15	0.95%	2.00	
Barclays	364 days	30/03/15	0.86%	1.00	14.50
Total			0.71%		32.37

Shaded investments represents term deposits made in the three months to 30th June 2014.

- 2.2 The council's current eligible UK counterparties, together with the maximum maturity periods (as recommended by the council's treasury advisers, Arlingclose), are as follows:

Counterparty	Maximum maturity period from:	
	01/04/14	01/07/14
Close Brothers Ltd	100 days	100 days
Santander UK	6 months	13 months
Nat West and RBS	Overnight	Overnight
Bank of Scotland and Lloyds TSB	12 months	13 months
Nationwide	12 months	13 months
Barclays	12 months	13 months
HSBC and Standard Chartered Bank	12 months	13 months

- 2.3 New European banking regulations came into force from 1st January 2014. The measures are to strengthen the banking sector's resilience to financial and economic shocks. Whilst the banks have to hold larger capital and liquidity buffers, they need to set aside less liquidity cover for deposits over 12 months and, in response, are tailoring products to reflect this. The result is a small pick-up in return for deposits between 12 and 13 months hence Arlingclose flexing the above limits to accommodate this.
- 2.4 The council has earned interest on its investments as follows:

Month	Amount invested		Average rate of interest earned		Amount of interest earned / Forecast £	Budget £	Actual Surplus / Forecast £
	Actual / Forecast £m	Budget £m	Actual / Forecast %	Budget %			
Apr-14	35.09	20	0.68	0.60%	19,439	10,000	9,439
May-14	40.21	40	0.63	0.60%	21,580	20,000	1,580
Jun-14	33.96	40	0.67	0.60%	18,815	20,000	-1,185
					59,834	50,000	9,834
Jul-14		40		0.60%	20,000	20,000	-
Aug-14		40		0.60%	20,000	20,000	-
Sep-14		40		0.60%	20,000	20,000	-
Oct-14		30		0.60%	15,000	15,000	-
Nov-14		30		0.60%	15,000	15,000	-
Dec-14		30		0.60%	15,000	15,000	-
Jan-15		20		0.60%	10,000	10,000	-
Feb-15		20		0.60%	10,000	10,000	-
Mar-15		10		0.60%	5,070	5,070	-
Budget and projected outturn					189,904	180,070	9,834

- 2.5 Investment balances in April were higher than budgeted resulting in a surplus for the month of £9,439. In the remainder of the year investment balances and/or rates of interest earned may be below the amounts budgeted and so at this stage in the year the forecast outturn is taken to be the same as the budget.

3. The Council's Borrowing

Short-term borrowing

- 3.1 The council is continuing its policy of utilising short-term borrowing from other local authorities to fund its capital programme and for short-term liquidity needs. These short-term interest rates are significantly below levels available from other sources.
- 3.2 Historically the council has always borrowed for longer periods at fixed interest rates. Whilst achieving stability in the amount of its interest payments, the council currently has a large cost of carry when comparing its fixed interest debt to current (variable) investment rates.
- 3.3 It is considered good practice to have an element of variable rate borrowing that removes or reduces this cost of carry and, to the extent that the level of short-term debt does not exceed the level of the council's investments, when interest rates rise increased investment income provides a hedge against increased borrowing costs.
- 3.4 The council can only borrow up to its Capital Financing Requirement, which represents the need to borrow for capital spend, and cannot borrow beyond this to finance the revenue budget.
- 3.5 At the end of June 2014 short-term borrowing from other local authorities consisted of seven loans totalling £24 million. Five loans totalling £14 million were taken out for 364 days at an average interest rate of 0.46% (including brokers commission) with the other two loans of £5 million each taken out for 87 days (at 0.36%) and 179 days (at 0.43%).

Long-term borrowing

- 3.6 No long-term loans have been taken out in the period to date.
- 3.7 The budget includes provision to take out up to £10 million of longer term loans from the Public Works Loan Board. This is still a possibility although analysis suggests that PWLB rates will have to fall significantly from their current levels for any savings in future years to outweigh the associated cost of carry in the short-term.
- 3.8 The current position is summarised below.

Summary of Borrowing Budget	Budget	Forecast	Savings
	£m	£m	£m
Minimum Revenue Provision	10.19	9.93	0.26
Interest on existing longer-term PWLB and bank loans	5.52	5.52	-
<u>Variable rate borrowing</u>			
<u>Budget</u> Borrowing required £68 million Rate 1.00%	0.55		

<u>Forecast</u> Borrowing required £60 million Average rate used 0.80%		0.29	0.26
<u>Fixed rate borrowing</u>			
<u>Budget</u> Provision for longer term-borrowing	0.10	0.10	-
Less capitalised interest (see 3.11 below)	(0.30)	(0.30)	-
Forecast savings compared to budget	16.06	15.54	0.52

3.9 The reduction in the Minimum Revenue Provision required for 2014/15 is due to slippage in the capital spend for 2013/14, as reported in June.

3.10 The external borrowing requirement is calculated after maximising internal borrowing by offsetting usable reserves. The usable reserves as at 31 March 2014 (of £41 million) were higher than forecast leading to an upward revision of the usable reserves available for 2014/15. The borrowing requirement shown above has been prudently calculated assuming usable reserves throughout the year of at least £30 million, whereas a figure of £20 million had previously been used.

3.11 The council is able to capitalise interest costs relating to interest paid on borrowing used to fund large capital schemes that take substantial periods of time to get to the point at which the assets may be utilised. Such interest, incurred at the construction or installation phase, may be added to the cost of the associated asset. As can be seen from the table above, capitalised interest of £300,000 has been included in the 2014/15 budget for capital financing costs.

4. Summary of Outturn Position

4.1 The current net treasury position, compared to budget, is estimated to be a surplus of at least £520,000.

Summary of Budget underspend	£m
Investment income receivable	-
Interest payable on borrowing	0.52
Total savings	0.52

4.2 The savings will be £100,000 greater if no longer-term fixed rate borrowing is taken out.

4.3 The savings will also be higher/lower if capitalised interest is more/less than £300,000.