Appendix 1

Annual Treasury Management Report 2016/17

1. Introduction

1.1. The council's treasury management activity is underpinned by CIPFA's Code of Practice on Treasury Management. Before the start of every year the Code requires local authorities to produce Prudential Indicators and a Treasury Management Strategy Statement detailing the policies and objectives of the council's treasury management activities for the forthcoming year. This outturn report compares actual activity to those policies and objectives.

1.2. The council borrows and invests substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of these risks are central to the treasury management strategy.

2. Economic Background

2.1. Two major events had a significant influence on financial markets during 2016/17; the UK EU referendum on 23 June and the election of President Trump in the USA on 9 November with both events resulting in uncertainties in economic market rates.

2.2. **Growth:** After a disappointing 2016 quarter 1 of only +0.2% GDP growth (GDP), the three subsequent quarters of 2016 came in at +0.6%, +0.5% and +0.7%, nearly the fastest rate of growth of any of the G7 countries.

2.3. **UK Monetary Policy**: On 4 August the Monetary Policy Committee (MPC) cut the bank rate from 0.5% to 0.25%, but remained at 0.25% for the rest of 2016/17.

2.4. **Inflation:** Inflation has risen rapidly due to the effects of the sharp devaluation of sterling after the referendum. In February 2017, the latest CPI inflation figure had risen to 2.3%, above the MPC's inflation target of 2%

3. Borrowing

3.1. The council continues to access lower cost short-term loans from other local authorities rather than more expensive longer term debt due to the differential between short and longer-term interest rates. This policy is expected to continue in 2017/18 but should this differential decrease and short term borrowing costs increase, the council will begin securing additional fixed long term debt to fund its borrowing requirements.

3.2. In 2016/17 the weighted average interest rate paid on council borrowing was 3.24% (3.42% in 2015/16). The weighted average cost of long term borrowing was 3.83% compared to 0.76% for short-term borrowing (being the gross cost including brokers' commission of between 0.03% and 0.10%).

3.3. It is council strategy to maintain borrowing and investments below their underlying levels by using "internal borrowing", utilising usable reserves. This maintains borrowing and investment balances to a minimum.

3.4. During 2016/17 there was major volatility in Public Works Loan Board (PWLB) rates with rates falling during quarters one and two to reach historically low levels, before rising significantly during quarter three and then partially easing back towards the end of the year. This enabled the council to replace some short-term loans with longer-term finance. In 2016/17 the following longer term loan was taken out from the PWLB:

Amount Borrowed	From	To	Period	Type of loan*	Interest Rate
£7m	30/06/16	30/06/46	30 years	Maturity	2.45%
*Maturity = Interest only instalments every six months over the period of the loan, with the principal repaid at the end of the loan period.					

3.5. The premium charged by the PWLB for the early repayment of PWLB debt remained too expensive for existing loans in the council's portfolio to be repaid and rescheduled. No rescheduling activity was undertaken in 2016/17 and this will continue to be constantly considered.

3.6. Borrowing activity during the year is summarised below:

Borrowing Activity in 2016/17	**01/04/16 Balance £m**	**New Borrowing £m**	**Debt Maturing £m**	**31/03/17 Balance £m**
Short-term borrowing	46.50	51.00	(69.50)	28.00
Long-term borrowing	149.95	7.00	(8.46)	148.49
TOTAL BORROWING	**196.45**	**58.00**	**(77.96)**	**176.49**
Other long-term liabilities*	25.56	33.39	(1.21)	57.74
TOTAL EXTERNAL DEBT	**222.05**	**91.39**	**(79.17)**	**234.23**
**Other long term liabilities represent existing commitments under PFI arrangements included in the medium term financial strategy inclusive of the energy from waste plant which became operational during the year*				

3.7. Total borrowing decreased by £20.0m due to repayments exceeding the need to borrow to fund capital programme spend in 16/17.

3.8. The council's underlying need to borrow as measured by the Capital Financing Requirement (CFR). As at 31/03/2017 this totalled £305.8m. The difference of £71.6m between the CFR and total external debt represents internal borrowing from usable reserves and working capital alongside the outstanding loan balance with Mercia waste of £38.1m.

3.9. The council's capital financing costs in 2016/17 were as follows.

Capital financing costs for 2016/17:	**Budget**	**Outturn**	**Over / (under) spend**
	£m	**£m**	**£m**
Minimum Revenue Provision (provision for repayment of loan principal)	**10.7**	**10.7**	**-**
Interest payable on all loans	**6.4**	**6.1**	**(0.3)**

TOTAL	**17.1**	**16.8**	**(0.3)**

3.10. The variances to budget have arisen from:

- Short-term variable interest rates being lower than expected resulting in an interest cost saving

4. Investments

4.1. The council invests significant funds, representing income received in advance of expenditure plus balances and reserves. During 2016/17 the council's investment balances averaged at £15m and ranged from £30m in December 2016 to £2m in February 2017.

4.2. Security of capital remained the council's primary objective. Investment income remained low due to the continued low interest rate environment.

4.3. Investments held at the start and end of the year were as follows:

Investments	01/04/16 Balance £m	Investments Made £m	Maturities/ Withdrawals £m	31/03/17 Balance £m
Instant Access Accounts	5.00	281.71	(283.74)	2.97
Notice Accounts	2.50	-	(2.50)	-
Total	**7.50**	**281.71**	**(286.24)**	**2.97**
Decrease in investments				**4.53**

4.4. Interest received during the year was as follows:

Month	Average amount invested		Average rate of interest earned		Budget	Interest earned	(Surplus) /deficit
	Actual £m	Budget £m	Actual %	Budget %	£000	£000	£000
Apr-16	13.4	30	0.61	0.40	10	6	(4)
May-16	13.1	30	0.50	0.40	10	6	(4)
Jun-16	16.3	30	0.49	0.40	10	6	(4)
Jul-16	19.2	30	0.49	0.40	10	8	(2)
Aug-16	13.8	30	0.42	0.40	10	5	(5)
Sep-16	12.2	30	0.36	0.40	10	4	(6)
Oct-16	13.4	30	0.32	0.40	10	4	(6)
Nov-16	23.8	30	0.27	0.40	10	5	(5)
Dec-16	19.2	30	0.27	0.40	10	4	(6)
Jan-17	13.9	30	0.28	0.40	10	3	(7)
Feb-17	8.9	30	0.29	0.40	10	2	(8)
Mar-17	7.2	30	0.29	0.40	10	2	(8)

Outturn	**120**	**55**	**(65)**

4.5. The interest received in the year was below budget due to lower balances being maintained, reducing the need to borrow.

4.6. The average interest rate achieved during 2016/17 was 0.38%, slightly lower than budgeted. This compares favourably with the generally accepted benchmark of the average 7-day London Inter-Bank Bid (LIBID) rate of 0.20%.

4.7. In addition to interest earned on balances, interest from the energy from waste plant loan to Mercia waste, totalling £2.3m, has been set aside to fund increased waste disposal costs in future years.

5. Compliance with Prudential Indicators

5.1. The Council complied with its Prudential Indicators, Treasury Management Policy Statement and Treasury Management Practices for 2016/17 as detailed in Annex 1. A prudent approach has been taken in relation to investment activity with priority being given to security and liquidity over yield.

Appendix 1

Annual Treasury Management Report 2016/17

Annex 1

Performance Indicators

1. Treasury Management Indicators

The council measures and manages its exposures to treasury management risks using the following indicators.

1.1 Interest Rate Exposures

This indicator is set to control the council's exposure to interest rate risk. The indicator sets upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of net principal borrowed.

	2016/17 Approved Limit	2016/17 maximum exposure
Upper Limit for Fixed Rate Exposure	100%	100%
Upper Limit for Variable Rate Exposure	50%	22%

The above indicator relates to net debt, if the council has variable rate investments at the same level as its variable rate debt it is deemed to have no variable rate exposure (all council investments are regarded as being at variable rate because no investments are for more than one year). Throughout 2016/17 the council's investments were lower than its variable rate short-term borrowing.

1.2 Maturity Structure of Fixed Rate Borrowing

This indicator is to limit large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates.

Maturity Structure of Fixed Rate Borrowing	Lower Limit %	Upper Limit %	Actual Fixed Rate Borrowing 31/03/17 £m	% Fixed Rate Borrowing 31/03/17
Under 12 months	0%	20%	**5.48**	**4%**
12 months and within 24 months	0%	20%	**5.49**	**4%**
24 months and within 5 years	0%	20%	**13.09**	**9%**
5 years and within 10 years	0%	20%	**27.83**	**19%**
10 years and within 20 years	0%	40%	**28.48**	**19%**
20 years and within 30 years	0%	40%	**25.86**	**17%**
30 years and within 40 years	0%	40%	**22.26**	**15%**
40 years and within 50 years	0%	40%	**20.00**	**13%**
Total			**148.49**	**100%**

Two LOBO ("Lenders Option then Borrowers Option") bank loans of £6m each are repayable in 2054 however if the lenders seek to increase the interest rate charged, currently 4.50%, the council has the opportunity to repay the loans.

1.3 Upper Limit for Total Principal Sums Invested Over 364 Days

The purpose of this limit is to contain exposure to the possibility of financial loss that may arise as a result of the council having to seek early repayment of the sums invested.

Appendix 1

Annual Treasury Management Report 2016/17

Upper Limit for Total Principal Sums Invested Over 364 Days	2016/17 Approved £m	2016/17 Actual £m	2017/18 Estimate £m	2018/19 Estimate £m
Total	**5**	**0**	**5**	**5**

During 2016/17 no long-term investments were made for a period exceeding 364 days.

2. Prudential Indicators

2.1 Estimates of Capital Expenditure

This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on council tax.

Capital Expenditure	2016/17		2017/18	2018/19
	Estimate £000	Actual £000	Estimate £000	Estimate £000
Total	**75,075**	**55,785**	**73,272**	**65,938**

Capital expenditure has been and is expected to be financed or funded as follows:

Capital Financing	2016/17		2017/18	2018//19
	Estimate £000	Actual £000	Estimate £000	Estimate £000
Capital grants	24,343	33,628	39,071	41,082
Capital receipts	7,900	2,092	9,745	2,125
Revenue funding	-	495	-	-
Prudential borrowing	42,532	19,570	24,456	22,731
Other	300	-	-	-
Total	**75,075**	**55,785**	**73,272**	**65,938**

Generally prudential borrowing finance is provided where the return on the investment exceeds the debt financing cost.

3. Capital Financing Requirement (CFR)

Estimates of the council's cumulative maximum external borrowing requirement for 2016/17 to 2018/19 are shown in the table below:

Capital Financing Requirement	2016/17 Approved £000	**2016/17 Actual £000**	2017/18 Estimate £000	2018/19 Estimate £000
Total CFR	**316,677**	**305,828**	**209,552**	**224,174**

Total debt is expected to remain at or below the CFR during the forecast period.

Annual Treasury Management Report 2016/17

4. Authorised Limit and Operational Boundary for External Debt

The Local Government Act 2003 requires the Council to set an Affordable Borrowing Limit or Authorised Limit. This is a statutory limit which should not be breached.

The Operational Boundary is based on the same estimates as the Authorised Limit but reflects the most likely, prudent but not worst case scenario without the additional headroom included within the Authorised Limit.

	2016/17 Approved Operational Boundary £m	**2016/17 Approved Authorised Limit £m**	**Actual External Debt as at 31/03/17 £m**
Borrowing	295.0	305.0	176.5
Other Long-term Liabilities	30.0	40.0	57.7
Total	**325.0**	**345.0**	**234.2**

5. Ratio of Financing Costs to Net Revenue Stream

This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

Ratio of Financing Costs to Net Revenue Stream	**2016/17 Approved %**	**2016/17 Actual %**	**2017/18 Estimate %**	**2018/19 Estimate %**
Net Revenue Stream	143,529	147,979	**145,025**	**141,641**
Financing Costs	17,096	16,771	**17,859**	**17,750**
Percentage	**11.9%**	**11.3%**	**12.3%**	**12.5%**

6. Adoption of the CIPFA Treasury Management Code

This indicator demonstrates that the council has adopted the principles of best practice.

The council has incorporated the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2011 Edition* into its treasury policies, procedures and practices.