Report of the Director
of Governance and Partnerships

Agenda Item No: 7
Meeting: 11 April 2017

NORTH LINCOLNSHIRE COUNCIL

AUDIT COMMITTEE

**TREASURY MANAGEMENT AND INVESTMENT STRATEGY
PERIOD 11 UPDATE**

1. OBJECT AND KEY POINTS IN THIS REPORT

1.1. To inform the Audit Committee of the current position in respect of the Council's Treasury Management Strategy and its performance.

1.2. The report covers

- The legal and regulatory framework
- The council's strategy
- Period11 Review

1.3. The key points are that

- The base rate was reduced to 0.25% in 2016, which means lower interest received from council investments
- The Council has an on-going need to borrow to finance its capital programme. The council will undertake Long Term borrowing at the most appropriate point in the year and utilise its capacity to undertake short term borrowing.
- The Council has accessed the intra-Local Authority lending market as a means of funding its short-term borrowing requirement at well below PWLB rates.

2. BACKGROUND INFORMATION

The legal and regulatory framework

2.1. The annual treasury management and investment strategy was prepared in line with

- CIPFA Code of Practice in the Public Service Fully Revised 2011
- CIPFA The Prudential Code Fully Revised Second Edition 2011
- DCLG Guidance
- Local Government Act 2003

2.2. The code of practice requires that Full Council receive a report on treasury management strategy at the start of the financial year, at mid-year and at year end. The Audit Committee receives progress reports at each meeting and an annual report on the outturn position.

2.3. It also requires the Council to maintain suitable Treasury Management Practices (TMPs), setting out the manner in which the organisation will seek to achieve its Treasury Management policies and objectives, and prescribing how it will manage and control those activities. As part of this ongoing process the Treasury Management Practices are reviewed on a regular basis.

3. OPTIONS FOR CONSIDERATION

3.1. There are no options for consideration. However the performance against the approved strategy can be evaluated. The annual strategy covers:

- the investment strategy
- the borrowing strategy
- and the prudential indicators for external debt and treasury management.

The Strategy for 2016-17

3.2. The strategy for 2016/17 was based on the council's views on interest rates and appropriate counterparties for investment and borrowing based on experience, market intelligence including that provided by credit rating agencies, brokers, advisors and the financial press.

The key projections were:

- An average bank base rate of 0.5% (£50k target)
- An average loan rate of 4%

The Investment Strategy

3.3. The Investment strategy for 2016/17 aimed to reduce risk by;

- Maintaining a low level of cash balances consistent with ensuring adequate liquidity, although this increases exposure to liquidity risk
- Limiting the maximum investment period to twelve months
- Applying a maximum investment limit of £7m or lower for counter-parties (except the council’s own bankers)
- Applying a maximum limit to financial groups rather than separate institutions
- Investing in a range of financial institutions including UK institutions with a minimum of an adequate credit rating or equivalent and Money Market Funds.
- Investing in additional instruments such as Certificates of Deposit

.

(see Appendix 1 for list of approved counterparties)

The Borrowing Strategy

3.4. The Borrowing Strategy for 2016/17 aimed to;

- Borrow at the most advantageous point possible
- Track short-and long-term interest rates alongside investment rates to determine that point
- Consider borrowing from a range of institutions to ensure the best value for money
- Generally borrow only to support the capital programme
- Borrow for shorter periods if cash flow requires or to avoid long term borrowing for a period.

Period 11 REVIEW 2016/17

3.5. The council's treasury operations take place in the context of the wider national and international economy. Events in financial markets therefore can have an impact on the council. No treasury activity is without risk, and risks include credit risk (cost of borrowing and exposure to the market, liquidity risk (ensuring cash balances are sufficient to meet the day to day needs of the council), interest rate risk(on borrowing and investments) and reputational risk. The Authority has access to data tools that are used to monitor these risks and used to inform investment and borrowing decisions.

3.6. A number of these risk factors are considered below.

- Markets are taking a 'wait and see' approach to EU withdrawal and gilt yields are now roughly back where they were before the EU referendum.

- The Council for a number of years eliminated credit risk by using cash reserves (internal borrowing) instead of building cash balances through external borrowing. However cash balances have been fully utilised and in 2015/16 and 2016/17 the Council has needed to borrow to fund its capital programme and to maintain liquidity. It will need to continue do so in the years ahead.

- At the end of February 2017 the Authority had £126.689m of long term borrowing, £17m of short term borrowing and £6.25m of investments. The most efficient source of funds is the intra-Local Authority market and these have been used to provide flexible and low interest rate borrowing. Details are shown in Appendix 1.

- Investment balances have ranged from £13.9m down to £1.0m over the period. With changes in cash requirements of up to £10m over a few days, target average balances are maintained c£4m-£10m using the short term loan market.

- Average return on invested funds during the period was low 0.15 %. The average rate for 2016/17 so far is 0.21%. This reflects the low interest rate environment and the policy of keeping low balances and prioritising liquidity.

- We continue to use the CCLA Money Market Fund to diversify across a range of counterparties, more than we could access ourselves directly. Deposits were kept well within the TMSS limit of £5m. Details of investments at the end of February are shown in the table:

Counterparty Name	Avg Rate	Principal O/S	Avg Duration
National Westminster Bank plc	0.01%	£5,888	0
Lloyds Bank plc	0.15%	£244	0
Barclays Bank plc	0.20%	£4,748,277	0
CCLA The Public Sector Deposit 4	0.26%	£1,500,000	0
Totals	**0.15%**	**£6,254,409**	0

- The latest prudential indicator data is shown at Appendix 2.

4. ANALYSIS OF OPTIONS

4.1 This is a report on past performance and there are no options to consider.

4.2 The borrowing decisions made were taken after review of the most appropriate options in terms of value, tenure and fit with our projected short and long terms needs.

5. RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY, IT)

5.1 The financial implications to this report are covered in section 3.

5.2 Staff time has been effectively dedicated to the gathering of intelligence and the building up of research capacity to aid, sustain and inform the treasury management function in making borrowing and investment decisions.

6. OUTCOMES OF INTEGRATED IMPACT ASSESSMENT (IF APPLICABLE)

6.1 Not applicable

7. OUTCOMES OF CONSULTATION AND CONFLICTS OF INTERESTS DECLARED

7.1 Not applicable

8. RECOMMENDATIONS

8.1 That the Audit Committee considers the assurance provided by this report on the effectiveness of arrangements for treasury management, and:

8.2 That the Audit Committee notes the Period 11 Treasury Management performance for the 2016/17 financial year.

DIRECTOR OF GOVERNANCE AND PARTNERSHIPS

Civic Centre
Ashby Road
SCUNTHORPE
North Lincolnshire
DN16 1AB
Author: Rachel Carey/Mark Kitching
Date: 23/3/17

Background Papers used in the preparation of this report

CIPFA Code of Practice in the Public Service Fully Revised 2011
CIPFA The Prudential Code Fully Revised Second Edition 2011
DCLG Guidance
Local Government Act 2003

Appendix 1

COUNTERPARTY LIST

BANKS	**Fitch**		**Moody's**		**Standard & Poor's**		**Counterparty Limit**
	ST	**LT**	**ST**	**LT**	**ST**	**LT**	**£**
United Kingdom							
Barclays Bank	F1	A	P1	A2	A-2	A	£14,000,000
HSBC Bank plc	F1+	AA-	P1	Aa2	A-1+	AA-	£7,000,000
Santander UK	F1	A	P1	Aa3	A-1	A	£7,000,000
Standard Chartered Bank	F1	A+	P1	Aa3	A-1	A	£7,000,000
Lloyds Banking Group							£7,000,000
Bank of Scotland	F1	A+	P1	A1	A-1	A	
Lloyds Bank	F1	A+	P1	A1	A-1	A	
RBS Group							£4,000,000
National Westminster Bank	F2	BBB+	P2	A3	A-2	BBB+	
Royal Bank of Scotland	F2	BBB+	P2	A3	A-2	BBB+	

BUILDING SOCIETIES	**Fitch**		**Moody's**		**Standard & Poor's**		**Counterparty Limit**
	ST	**LT**	**ST**	**LT**	**ST**	**LT**	**£**
Nationwide	F1	A	P1	A1	A-1	A	£7,000,000
Coventry	F1	A	P1	A2			£4,000,000
Leeds	F1	A-	P1	A2			£4,000,000
Principality	F2	BBB+	P3	Baa3			£4,000,000
Skipton	F2	BBB+	P2	Baa2			£4,000,000
Yorkshire	F1	A-	P2	A3			£4,000,000

GOVERNMENT INSTITUTIONS							
Debt Management Office							Unlimited
Local authorities							
District Council's							£3,000,000
All Other LA's							£5,000,000
Fire Authorities							£5,000,000
Police authorities							£5,000,000

MONEY MARKET FUND	**Fitch**	**Moody's**	**Standard & Poor's**
Funds rated by at least one agency as:	AAAMmf	Aaa-mf	AAAm

NAME	START DATE	AMOUNT	% INTEREST RATE	MATURITY DATE
West Yorkshire Combined Authority	11/04/2016	£5,000,000.00	0.35	22/04/2016
Shropshire Fire and Rescue Service	23/05/2016	£2,000,000.00	0.38	23/06/2016
Greater Manchester Combined Authority	23/05/2016	£5,000,000.00	0.38	23/06/2016
Manchester City Council	03/06/2016	£3,000,000.00	0.38	01/07/2016
Greater Manchester Combined Authority	23/06/2016	£5,000,000.00	0.38	25/07/2016
Sheffield City Region Combined Authority	23/06/2016	£5,000,000.00	0.60	23/03/2017
Manchester City Council	01/07/2016	£3,000,000.00	0.38	01/08/2016
Basildon Borough Council	06/07/2016	£2,000,000.00	0.47	07/11/2016
Vale of Glamorgan Council	06/07/2016	£2,000,000.00	0.50	06/01/2017
West Yorkshire Police Commissioner	06/07/2016	£3,000,000.00	0.55	06/02/2017
Middlesbrough Council	29/09/2016	£3,000,000.00	0.20	06/10/2016
Portsmouth City Council	25/11/2016	£3,000,000.00	0.32	02/12/2016
Cheshire West and Chester Council	19/12/2016	£3,000,000.00	0.28	19/01/2017
Edinburgh City Council	23/12/2016	£4,000,000.00	0.36	04/01/2017
Cheshire West and Chester Council	19/01/2017	£3,000,000.00	0.22	20/02/2017
Leicester City Council	27/01/2017	£3,000,000.00	0.35	20/03/2017
Cheshire West and Chester Council	20/02/2017	£6,000,000.00	0.23	17/03/2017
Middlesbrough Council	24/02/2017	£3,000,000.00	0.33	17/03/2017

Appendix 2

Prudential Indicators

Treasury Management Indicators
The Authority measures and manages its exposures to treasury management risks using the following indicators.

Interest Rate Exposures: This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of net principal borrowed for 2016/19 are:

	2016/17	2017/18	2018/19
Upper % limit on fixed interest rate exposure	100%	100%	100%
Actual	86%	-	-
Upper % limit on variable interest rate exposure	20%	20%	20%
Actual %	14%	-	-

Maturities falling within 12 months are classed as 'variable rate' as they are exposed to short-term rate fluctuations should they need to be replaced on maturity.

Maturity Structure of Borrowing: This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing for 2016/17 are:

	Upper	Lower	Actual
Under 12 months	20%	0%	14%
12 months and within 24 months	15%	0%	5%
24 months and within 5 years	50%	0%	3%
5 years and within 10 years	75%	0%	22%
Over 10 years	90%	25%	56%

Principal Sums Invested for Periods Longer than 365 days: The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by needing to seek early repayment of its investments. This could occur as a result of a credit event or a change in cash flow circumstances. The council did not invest for longer than 365 days during the period.

Other Prudential Indicators
The following three prudential indicators are relevant to the treasury function as they concern limits on borrowing and the adoption of the CIPFA Treasury Management Code.

Operational Boundary for External Debt: The operational boundary is based on the Authority's estimate of most likely, i.e. prudent, but not worst case scenario for external debt.

Operational Boundary	2016/17 £m	2017/18 £m	2018/19 £m
Borrowing	£205m	£202m	£196m
Other long-term liabilities	£2m	£2m	£2m
Total Debt	£207m	£204m	£198m

Authorised Limit for External Debt: The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Authority can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

Authorised Limit	2016/17 £m	2017/18 £m	2018/19 £m
Borrowing	£257m	£254m	£247m
Other long-term liabilities	£5m	£5m	£5m
Total Debt	£262m	£259m	£252m

Adoption of the CIPFA Treasury Management Code: The Authority adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition in February 2012.

Other Matters

All Treasury Activity is now undertaken through the joint service with North East Lincolnshire Council. Now that the final structure and new systems and process have been introduced the Treasury Management Practices (TMP's) have been updated to reflect the new arrangements.