Report to:	**Executive**
Date:	**10 September 2015**
Title:	**ANNUAL TREASURY MANAGEMENT REPORT 2014/15**
Portfolio Area:	**Support Services**
Wards Affected:	**ALL**

Urgent Decision:	**N**	Approval and clearance obtained:	**Y**

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Recommendations:

That the Executive

1. Approves the actual 2014/15 prudential and treasury indicators in this report

2. Notes the Annual Treasury Management Report for 2014/15

1. Executive summary

Income from investments this year was £137,000 which is £27,000 higher than the budget of £110,000 at an average return of 0.57%. The comparable performance indicator (Benchmark) is the average 7-day LIBID rate which was 0.35%. Therefore the Council achieved 0.22% return on investments over the benchmark for 14/15.

2. Background

Introduction

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2014/15. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

Treasury management is defined as:

"The management of the local authority's 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 "

During 2014/15 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Executive 06/03/2014 – E75/13)
- a mid-year (minimum) treasury update report (Council 23/10/2014 – E37/14)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Executive Committee before they were reported to the full Council.

The Economy and Interest Rates

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 much faster than expected 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 buoyant 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.

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.

Overall Treasury Position as at 31 March 2015

At the beginning and the end of 2014/15 the Council's treasury position was as follows:

	As at 31/03/2014		**As at 31/03/2015**	
	Principal	**Interest**	**Principal**	**Interest**
	£	**%**	**£**	**%**
Investment Type				
Call Account	-	-	400,000	0.30
Short Fixed	15,000,000	0.64	15,000,000	0.64
Money Market Funds	2,950,000	0.33	5,750,000	0.40
Heritable Bank	72,368	-	72,368	-
Total	**18,022,368**	**0.59**	**21,222,368**	**0.57**

The Following is a list of our fixed investments at 31 March 2015

	Fixed to	**£**	**Interest Rate**
Barclays Bank	30/04/2015	5,000,000	0.32%
Nationwide B S	07/08/2015	5,000,000	0.66%
Lloyds Bank	03/09/2015	5,000,000	0.95%

Icelandic Bank

The Council placed a deposit of £1,250,000 on 25th September 2008 with the Heritable Bank which is a subsidiary of Landsbanki, one of the Icelandic Banks that was affected by the world economic crisis. Of this amount £1,177,632 (94%) has already been repaid to the Council by the Administrators. At the 31 March 2015, the Council had £72,368 frozen in the Heritable Bank.

At the time the deposit was placed, the risk rating of Heritable was 'A' (long term deposits) and F1 (short term deposits). Both ratings indicated low risk and were within the deposit policy approved by the Council. Heritable Bank is registered in Scotland with an address in Edinburgh. Heritable Bank Plc is authorised and regulated by the Financial Services Authority and is on the FSA Register. The bank's shares are owned by Icelandic bank, Landsbanki.

Administrators have kept the bank trading and are winding down the business over a period of years. The Administrators have paid fourteen dividends amounting to 94% of the original deposit. The Council has recently received a letter from the administrators advising that they intend to make a 15th dividend to be declared and paid in August 2015. The administrators estimate that the return to all unsecured creditors is now between 98-100 pence in the pound.

The Strategy for 2014/15

The Treasury Management Strategy is risk averse with no investments allowed for a period of more than a year and very high credit ratings are required together with a limit of £5m per counterparty. This has resulted in only a small number of institutions in which we can invest (see Appendix A).

Investment Rates in 2014/15

Bank Rate remained at its 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.

Investment Outturn for 2014/15

Investment Policy – the Council's investment policy is governed by the Department for Communities and Local Government (DCLG) guidance, which has been implemented in the annual investment strategy approved by the Executive on 06/03/2014. This policy sets 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.).

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Investments held by the Council - Income from investments this year was £137,000 which is £27,000 higher than the budget of £110,000 at an average return of 0.57%. The comparable performance indicator (Benchmark) is the average 7-day LIBID rate which was 0.35%. Therefore the Council achieved 0.22% return on investments over the benchmark for 14/15.

3. Implications

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/Governance	Y	Statutory powers are provided by the Local Government Act 1972 Section 151 and the Local Government Act 2003
Financial	Y	Income from Treasury Management activities amounted to £137,000 in 2014/15. Consideration of the Annual Treasury Report forms an essential component of the Council's systems for public accountability. It also provides a platform for future investment planning.
Risk	Y	The security risk is the risk of failure of a counterparty. The liquidity risk is that there are liquidity constraints that affect the interest rate performance. The yield risk is regarding the volatility of interest rates/inflation. The Council has adopted the CIPFA Code Of Practice for Treasury Management and produces an Annual Treasury Management Strategy and Investment Strategy in accordance with CIPFA guidelines. The Council engages a Treasury Management advisor and a prudent view is always taken regarding future interest rate movements. Investment interest income is reported quarterly to SLT and the Executive.

Comprehensive Impact Assessment Implications		
Equality and Diversity	N	N/a
Safeguarding	N	N/a
Community Safety, Crime and Disorder	N	N/a
Health, Safety and Wellbeing	N	N/a
Other implications	N	none

Supporting Information

Appendices:

Appendix A – Lending list as at 31 March 2015
Appendix B – Prudential and Treasury Indicators 2014/15

Background Papers:

Annual treasury strategy in advance of the year (Executive 06/03/2014 – E75/13)
A mid-year (minimum) treasury update report (Council 23/10/2014 – E37/14)

Approval and clearance of report

Process checklist	Completed
Portfolio Holder briefed	**Yes**
SLT Rep briefed	**Yes**
Relevant Exec Director sign off (draft)	**Yes**
Data protection issues considered	**Yes**
If exempt information, public (part 1) report also drafted. (Committee/Scrutiny)	**N/a**

APPENDIX A

SOUTH HAMS DISTRICT COUNCIL LENDING LIST AS AT 31 MARCH 2015.

Barclays Bank Plc
HSBC Bank plc
Lloyds Banking Group Plc: • Bank of Scotland plc • Lloyds TSB Bank plc
Nationwide Building Society
Royal Bank of Scotland Group Plc: • The Royal Bank of Scotland plc • National Westminster Bank plc
Government UK Debt Management Facility
Local Authorities (as defined under Section 23 of the Local Government Act 2003)
AAA rated Money Market Funds

APPENDIX B

PRUDENTIAL AND TREASURY INDICATORS 2014/15

CAPITAL PRUDENTIAL INDICATORS

The Council's capital expenditure plans are the key driver of treasury management activity. The outputs of the capital expenditure plans are reflected in prudential indicators, which are designed to assist members to overview and confirm capital expenditure plans.

Capital Expenditure.

This prudential Indicator is a summary of the Council's capital expenditure.

Capital Expenditure	2013/14 Actual £000	2014/15 Estimate £000	2014/15 Actual £000
Total spend	**4,040**	**2,377**	**3,554**

The table below summarises the financing of the Council's capital programme. Any shortfall of resources would result in a funding need (borrowing). However, the Council is currently debt-free.

Capital Expenditure	2013/14 Actual £000	2014/15 Estimate £000	2014/15 Actual £000
Total spend	**4,040**	**2,377**	**3,554**
Financed by:			
Capital receipts	1,455	1,095	542
Capital grants	1,549	282	1,604
Revenue reserves	1,036	1,000	1,408
Total funding	**4,040**	**2,377**	**3,554**

Nb. Please note that the estimate for 2014-15 represents the approved capital programme for that year. However, actual capital spend includes not only expenditure on projects within that capital programme, but also expenditure on schemes carried forward from previous capital programmes.

The Council's Borrowing Need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). It is essentially a measure of the Council's underlying need to borrow if the figure is greater than zero. The negative figure reflects the fact that the Council is debt-free and has a nil borrowing requirement.

	2013/14 Actual £000	2014/15 Estimate £000	2014/15 Actual £000
Total CFR	**(98)**	**(98)**	**(98)**
Movement in CFR	**Nil**	**Nil**	**Nil**
Net borrowing requirement (the Council is debt free)	**Nil**	**Nil**	**Nil**

AFFORDABILITY PRUDENTIAL INDICATORS

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

Ratio of financing costs to net revenue stream

This indicator identifies the trend in the receipt of net investment income against the net revenue stream. It is calculated by dividing investment income and interest received by the Council's Net Budget.

	2013/14 Actual	2014/15 Estimate	2014/15 Actual
Ratio of net investment income to net revenue stream (surplus).	1.8%	1.2%	1.5%

Estimates of the incremental impact of capital investment decisions on council tax

This indicator calculates the notional cost of the impact of lost investment income on the Council Tax, from spending capital resources.

Incremental impact of capital investment decisions on the band D council tax (notional cost as explained above

	2013/14 Actual £	2014/15 Estimate £	2014/15 Actual £
Future incremental impact of capital investment decisions on the Band D council tax (Notional cost)	0.30	0.14	0.21

TREASURY INDICATORS: LIMITS TO BORROWING ACTIVITY

The Operational Boundary – This is the limit beyond which external debt is not normally expected to exceed. This is the maximum level of external debt for cash flow purposes.

Operational Boundary	2013/14 £	2014/15 £
Borrowing	2,000,000	2,000,000
Other long term liabilities	-	-
Total	2,000,000	2,000,000

The Authorised Limit for External Debt – A further key prudential indicator represents a control on the overall level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by Full Council. It reflects the level of external debt which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

This provides headroom over and above the operational boundary for unusual cash movements. This is the maximum amount of money that the Council could afford to borrow.

This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although no control has yet been exercised.

Authorised limit	2013/14 £	2014/15 £
Borrowing	7,000,000	7,000,000
Other long term liabilities	-	-
Total	7,000,000	7,000,000