Committee report

SPT

Mid-Year Treasury Management Report 2016/17

Committee Strategy and Programmes

Date of meeting 11 November 2016 **Date of report** 1 November 2016

Report by Assistant Chief Executive (Business Support)

1. Object of report

SPT is required through regulations issued under the Local Government in Scotland Act 2003 to produce a mid-year report reviewing treasury management activities undertaken in the first half of the financial year. 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).

2. Background

SPT has adopted the CIPFA Code of Practice on Treasury Management and fully complies with its requirements.

The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of SPT's treasury management activities.
- Creation and maintenance of Treasury Management Practices which set out the manner in which SPT will seek to achieve those policies and objectives.
- Receipt by the Partnership of an annual strategy report for the year ahead and an annual review report of the previous year.
- Delegation by SPT of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

Treasury management in this context 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 the optimum performance consistent with those risks."

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 an update on treasury activities and highlights compliance with the Partnership's policies previously approved by members.

3. The Economy and Interest Rates

3.1 Economic performance to date and outlook

Economic growth (GDP) was 2.2% higher in Quarter 2 (April to June) 2016 compared with the same quarter a year ago. Following the referendum vote for Brexit in June, the Bank of England forecast for growth for 2016 remained unchanged at 2.0% but the forecast for 2017 was cut from 2.3% to 0.8%.

The Bank of England meeting in August addressed this slowdown in forecast growth by a package of measures including a cut in Bank Rate from 0.50% to 0.25%. The expectation is for a further reduction in Bank Rate to 0.10% in December 2016 and to remain at this level until Quarter 2 2018.

The challenging investment environment experienced in recent years has continued. The cut in Bank Rate has resulted in corresponding reductions in the interest rates earned by SPT on its current investments and consequently a reduction in income.

The longer term trend is still for Public Works Loan Board (PWLB) borrowing rates to rise gradually.

CPI inflation increased from 0.3% in April 2016 to 1.0% in September 2016, having remained at, or near to, 0% throughout the financial year 2015/16. This was mainly due to rising prices for clothing and motor fuel. The expectation is for inflation to continue to rise to around 2.4% in 2018 and 2019.

3.2 Capita Asset Services' forecast for Bank Rate interest

Table 1 below shows the forecast for Bank Rate interest provided by Capita Asset Services, SPT's treasury advisor.

Table 1										
Now	**Dec-16**	**Mar-17**	**Jun-17**	**Sep-17**	**Dec-17**	**Mar-18**	**Jun-18**	**Sep-18**	**Dec-18**	**Mar-19**
0.25%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.25%	0.25%	0.25%	0.25%

4. Treasury Management Strategy Update

The Treasury Management Strategy 2016/17, including the Annual Investment Strategy, was approved by the Strategy & Programmes Committee on 18 March 2016.

There are no proposed policy changes to the Treasury Management Strategy. The information in this report updates the position in light of the economic position and budgetary changes already approved.

5. Capital Position (Prudential Indicators)

The Partnership undertakes capital expenditure on long-term assets. These activities may be financed through the application of capital or revenue resources (e.g. capital grants, capital receipts, revenue contributions etc.) or give rise to a borrowing requirement.

This section of the report provides an update on:

- SPT's capital expenditure plans;
- how these plans are financed;
- the impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- compliance with the limits in place for borrowing activity.

5.1 Prudential Indicator for Capital Expenditure

The actual capital expenditure forms one of the required prudential indicators.

Table 2 below provides a summary of the revised capital expenditure plans for 2016/17 as approved by the Strategy & Programmes Committee on 9 September 2016.

Table 2	**Subway Mod £000**	**Subway Infrastructure £000**	**Fastlink £000**	**General Capital £000**	**Total £000**
Capital Programme approved by the Partnership on 4 March 2016	39,350	14,750	5,000	13,335	72,435
Amendments approved by the Strategy & Programmes Committee	-	-	-	60	60
Revised Capital Programme as at 9 September 2016	39,350	14,750	5,000	13,395	72,495

5.2 Changes to the financing of the capital programme

Table 3 below provides a summary of the available capital funding for 2016/17 as approved by the Partnership on 4 March 2016.

Table 3	**Subway Mod £000**	**Subway Infrastructure £000**	**Fastlink £000**	**General Capital £000**	**Total £000**
Scottish Government capital grants	26,000	-	5,000	10,034	41,034
Other grants and contributions	-	-	-	70	70
Revenue contribution to the capital programme	-	-	-	1,800	1,800
Available capital funding 2016/17	**26,000**	**-**	**5,000**	**11,904**	**42,904**

Subsequently, there has been a small increase (£60,000) in the contributions available for General Capital but these have been equalled by a corresponding increase in planned expenditure.

5.3 Revised capital programme position

Table 4 below provides a summary of the capital position as approved by the Strategy & Programmes Committee on 9 September 2016.

Table 4	**Subway Mod £000**	**Subway Infrastructure £000**	**Fastlink £000**	**General Capital £000**	**Total £000**
Revised Capital Programme as at 9 September 2016	39,350	14,750	5,000	13,395	72,495
Available capital funding 2016/17	26,000	-	5,000	11,964	42,964
Projected subway fund utilisation	-	14,750	-	-	14,750
Projected transfers from Unapplied Capital Grants	13,350	-	-	-	13,350
Projected variance	**-**	**-**	**-**	**1,431**	**1,431**

Further work to quantify and manage risk, advance savings and re-phase existing projects is being undertaken to balance spend against budget.

5.4 Changes to the Prudential Indicators for the Capital Financing Requirement, External Debt and the Operational Boundary

There are a number of prudential indicators that are reported to committee each year in relation to debt:-

- Capital Financing Requirement;
- Operational Boundary for External Debt and Authorised Limit for External Debt;
- Net Borrowing Requirement.

5.4.1 Capital Financing Requirement

The Capital Financing Requirement (CFR) is the amount of capital expenditure to be financed by means other than grants or capital receipts. As can be seen from Table 5 below, there has been no change in the CFR, reflecting the balanced changes in the Capital Programme and the Available Funding.

Table 5	**2016/17 Original Forecast £000**	**2016/17 Revised Forecast £000**
Capital Programme	72,435	72,495
Available Funding	71,004	71,064
Capital Receipts Reserve	1,431	1,431
Capital Financing Requirement	0	0

5.4.2 Operational Boundary for External Debt and Authorised Limit for External Debt

The Operational Boundary for external debt is the expected debt position taking account of all known factors. The Authorised Limit for External Debt represents the limit beyond which borrowing is prohibited, and needs to be set and revised by committee approval. As can be seen from Table 6 below, the Operational Boundary and Authorised Limit on External Debt have not changed from the original estimates.

Table 6	2016/17 Original Forecast £000	2016/17 Revised Forecast £000
Operational Boundary	20,000	20,000
Authorised Limit for External Debt	22,000	22,000

5.4.3 Net Borrowing Requirement

The Net Borrowing Requirement is a key control over the treasury activity to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. Net external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2016/17 and next two financial years. As can be seen from Table 7 below, SPT is currently a net investor.

Table 7	2016/17 Original Forecast £000	2016/17 Revised Forecast £000
Capital Financing Requirement	0	0
Less Investments	52,091	60,807
Net Borrowing Requirement	-52,091	-60,807

The revised investment forecast is based on current income and expenditure information projected to the end of the financial year.

6. Investment Strategy

The Treasury Management Strategy 2016/17 was reported to and approved by the Strategy & Programmes Committee on 18 March 2016.

In terms of investment policy, the 2016/17 Strategy states that “SPT’s investment priorities will be security first, liquidity second and then return.” During the first six months of 2016/17 this investment policy was followed in full.

In terms of creditworthiness, SPT applies the service provided by our treasury advisors, Capita Asset Services, for choosing investment counterparties. This creditworthiness service employs a modelling approach utilising credit ratings from the three main credit rating agencies supplemented by additional market data. During the first six months of 2016/17 this creditworthiness policy was followed in full and there were no liquidity difficulties.

In terms of permitted investments, SPT’s policy is governed by the Investment Regulations (Code on the Investment of Money by Local Authorities). The 2016/17 Strategy lists the

types of investments which can be used and sets appropriate limits for the amount that can be held in each investment type. During the first six months of 2016/17 this policy was followed in full.
In terms of counterparty limits the 2016/17 Strategy set these as follows:

- Principal Banker - the greater of £50m or 50% of total balances;
- UK Nationalised and Part Nationalised Banks - the greater of £30m or 30% of total balances;
- Other Institutions - the greater of £10m or 25% of total balances; and
- To allow for temporary operational circumstances, there is a tolerance level of 2% of the balance held with each counterparty.

During the first six months of 2016/17 this policy was followed in full.

7. Investment Outturn

The result of the investment strategy undertaken by SPT to Period 7 (ending 15 October 2016) is shown in the Table 8 below.

Table 8	Average Investment £000	Average Rate of Return %	Benchmark Return* %
Account 1	2,432	0.44	0.28
Account 2	10,000	0.66	0.28
Account 3	12,183	0.49	0.28
Account 4	681	0.10	0.28
Account 5	10,714	0.64	0.28
Account 6	11,074	0.59	0.28
Account 7	10,153	0.71	0.28
Account 8	0	0.00	0.28
Account 9	12,766	0.53	0.28
Account 10	9,525	0.83	0.28
Account 11	2	0.25	0.28
Account 12	73	0.25	0.28
Account 13	963	0.33	0.28
Account 14	5,012	0.58	0.28
Account 15	12,044	0.83	0.28

*The benchmark return is the 7 day LIBID uncompounded.

SPT earned interest of £0.4m during the first six months of 2016/17.

The overall average rate of return obtained equates to 0.64% per annum, which exceeds the benchmark by 0.36% per annum.

As can be seen from Table 8, SPT has a number of investment accounts with low balances. This is in order to maintain relationships with counterparties which currently offer low rates of return or do not meet the minimum acceptable credit quality. Retaining these accounts ensures quick access at the point that these accounts become competitive or regain the minimum acceptable credit quality.

8. Borrowing

As stated previously SPT had no requirement for new borrowing in the first six months of 2016/17 and remains debt free.

9. Conclusion

During the first half of 2016/17 SPT operated within the Treasury Limits and Prudential Indicators set out in the Treasury Management Strategy 2016/17.

10. Committee action

The Committee is recommended to note the content of this report.

11. Consequences

Policy consequences	*None.*
Legal consequences	*All legislation and regulations are adhered to.*
Financial consequences	*As detailed in the report.*
Personnel consequences	*None.*
Equalities consequences	*None.*
Risk consequences	*As detailed in the report.*

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