Report for:	**Cabinet**
Date of meeting:	**13 December 2016**
Part:	**I**
If Part II, reason:	

Title of report:	**Treasury Management 2016/17 Mid-Year Performance Report**
Contact:	Cllr Graeme Elliot – Portfolio Holder for Finance & Resources James Deane – Corporate Director (Finance & Operations) David Skinner – Assistant Director (Finance and Resources) Richard Baker – Group Manager (Financial Services)
Purpose of report:	To provide Members with mid-year information on Treasury Management performance.
Recommendations:	That Cabinet considers and agrees the half-year report on targets and performance, in Sections 4-7.
Corporate Objectives:	Dacorum Delivers – Optimising investment income for General Fund and Housing Revenue budgets whilst managing investment risk is fundamental to achieving the corporate objectives.
Implications: 'Value For Money' Implications:	<u>Financial</u> A summary of performance against the Council's budgeted investment income is included in Section 5 of the report. <u>Value for Money</u> The Council is required to invest surplus funds to ensure that it maximises the benefit of cash flows.
Risk Implications:	Failures in the banking sector have increased the risk of investment being lost. A prudent approach to investment is required to minimise the risk to the Council of investment losses. Currently all DBC investments are in prime UK banks or in UK Government bodies; such as the DMO and other local authorities.

Community Impact Assessment:	There are no community impact implications.
Health And Safety Implications:	There are no health and safety implications.
Monitoring Officer/S.151 Officer Comments:	**Monitoring Officer:** No comments to add to the report **S.151 Officer** This is a Section 151 Officer Report
Consultees:	Capita Asset Services
Background papers:	Treasury Management Strategy (Budget Report Appendix K) - Cabinet 9 February 2016
Glossary of acronyms and any other abbreviations used in this report:	Chartered Institute of Public Finance and Accountancy (CIPFA) Capital Financing Requirement (CFR) Gross Domestic Product (GDP) Monetary Policy Committee (MPC) Treasury Management Strategy Statement (TMSS) London Interbank Bid Rate (LIBID) Debt Management Office (DMO) Public Works Loan Board (PWLB) Housing Revenue Account (HRA)

1. Background

1.1 The Treasury Management team manages the Council's cash-flows in order to strike the optimal balance between the following three elements:

- The liquidity requirements for the Council's day-to-day business;
- Funding the Council's capital programme;
- Investing surplus monies in line with the Treasury Management Strategy.

1.2 The purpose of this report is to update Cabinet on the economic environment in which the Treasury team is operating, highlighting some of the key challenges, and to provide details of the current investment position (see Section 5).

2. Governance

2.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management 2011 (the Code) was adopted by this Council in 2011.

2.2 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 the Council's treasury management activities;

- Creation and maintenance of treasury management practices which set out the manner in which the Council will seek to achieve those policies and objectives;

- Receipt by the full council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year;

- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions;

- This organisation nominates Cabinet to be responsible for ensuring effective scrutiny of the Treasury Management Strategy, policies and monitoring before recommendation to Full Council.

Mid-year Report

2.3 This mid-year report has been prepared in compliance with the Code, and covers the following areas:

- An economic update for the first six months of 2016/17;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- A review of the Council's investment portfolio for 2016/17;
- A review of the Council's borrowing strategy for 2016/17;
- The Council's capital expenditure (prudential indicators).

3. Economic update

3.1 The commentary in this section reflects analysis provided by Capita Asset Services, the Council's treasury management advisers. It updates Members on the key factors around the economic conditions in which the Council is currently operating.

3.2 Following the referendum vote for Brexit in June 2016 there was an immediate shock fall in confidence indicators and business surveys, pointing to an impending sharp slowdown in the economy. However, subsequent surveys have shown a sharp recovery in confidence and business surveys. It is generally expected that although the economy will now avoid flat lining, growth will be weak through the second half of 2016 and in 2017.

3.3 Further to the amendments made to Treasury Management Strategy earlier in the year (Cabinet 13 July 2016 "Treasury Management Strategy Update"), Capita Asset Services have given advice to suggest investments only be placed in countries with a minimum sovereign rating of AA-. The UK continues to qualify using this credit criteria, as at the date of this report it's Sovereign rating was AA.

3.4 The Bank of England meeting on 4 August 2016 addressed the expected slowdown in growth by a package of measures including a cut in Bank Rate from 0.50% to 0.25%.

3.5 The Governor of the Bank of England, Mark Carney, had warned that a vote for Brexit would be likely to cause a slowing in growth, particularly from a reduction in business investment, due to the uncertainty of whether the UK would have continuing full access, (i.e. without tariffs), to the EU single market. He also suggested that the Government will need to help growth by increasing investment expenditure and possibly by using fiscal policy tools (taxation).

3.6 The Council's treasury advisor has provided the following rate forecasts. The budget and forecasts contained within the Medium Term Financial Strategy are based on these forecasts. Fluctuations in the bank rate will impact on investment returns. Fluctuations on the PWLB rates will directly impact on future borrowing costs.:

	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19
Bank rate	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.25%	0.25%	0.25%	0.25%	0.50%
5yr PWLB rate	1.00%	1.00%	1.10%	1.10%	1.10%	1.10%	1.20%	1.20%	1.20%	1.20%	1.30%
10yr PWLB rate	1.50%	1.50%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.70%	1.80%
25yr PWLB rate	2.30%	2.30%	2.40%	2.40%	2.40%	2.40%	2.50%	2.50%	2.50%	2.50%	2.60%
50yr PWLB rate	2.10%	2.10%	2.20%	2.20%	2.20%	2.20%	2.30%	2.30%	2.30%	2.30%	2.40%

4. Treasury Management Strategy Statement and Annual Investment Strategy update

4.1 The Treasury Management Strategy Statement (TMSS) for 2016/17 was approved by Council on 9 February 2016.

4.2 The Council's Annual Investment Strategy, which is incorporated within the TMSS, outlines the Council's investment priorities as follows:

- Security of capital;

- Liquidity;
- Return on investment.

4.3 The Council aims to achieve the optimum return on investments within the context of the first two priorities. A breakdown of the Council's investment portfolio, as at 30 September 2016, is shown in Appendix 1 of this report. Capita's full counterparty credit list as at September 2016, which identifies those organisations with which the Council is able to place funds, is shown in Appendix 2.

4.4 All the Councils Investments during the first six months of the year have been placed in accordance with the approved strategy.

5. Investment Portfolio 2016/17

5.1 The Bank of England base rate remains low (as outlined in section 3). Because of this, the market rates banks are willing to pay on investments also remains low.

5.2 The continuing potential for a re-emergence of a Eurozone sovereign debt crisis together with other risks which could impact on the creditworthiness of banks, prompts a low risk strategy. Given this risk environment, investment returns are likely to remain low.

5.3 The Council held £77.5m of investments as at 30 September 2016 (£69.21m at 31 March 2016). The investment return for the first six months of the year was 0.60 %.

5.4 The Council's investment return for Q1 and Q2 2016/17 displays a £10k favourable variance against half yearly budgeted figure of £224k. Although interest rates have decreased, the Council is holding higher than budgeted cash balances. These balances include the remaining £7m (of the £19.78m) that the Council borrowed from the PWLB in advance of need in order to take advantage of historically low interest rates. Another factor contributing to the increased balances is the level of Right to Buy receipts. The Government has continued to increase discounts and publicise the scheme, generating £7.3m in sales by the end of September, against a budget of £3.95m for half of the year. The scheme take up shows no signs of slowing down.

6. Borrowing

6.1 The Council's Capital Financing Requirement (CFR) is the Council's underlying need to borrow for capital purposes, and is currently forecast to be £359.693m as at 31/3/17. This includes the borrowing from the Public Works Loan Board (PWLB) following the introduction of HRA Self Financing, and the £19.7m borrowing taken up in 2015/16 for general fund capital expenditure requirements, referred to in paragraph 5.4.

6.2 As a Local Authority, the Council is able to borrow funds from PWLB, which operates within the Debt Management Office (DMO), an Executive Agency of HM Treasury.

6.3 The PWLB charges interest rates, which are linked to government gilts and are lower than the Council would be able to achieve by raising funds through the capital markets. Following completion of a voluntary return on future borrowing requirements, the Council can borrow at the ‘certainty rate’ for all new borrowing, which is 20 basis points below the published PWLB rates.

7. The Council’s Capital Expenditure (Prudential Indicators)

7.1 Prudential indicators are set each year as part of the Council’s Treasury Management Strategy. They set the annual limits on borrowing, and provide a basis for assessing the affordability of financing costs, external debt and capital expenditure.

7.2 This part of the report is structured to update:

- The Council’s capital expenditure plans;
- How these plans are being 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.

7.3 Prudential Indicators for Capital Expenditure:

The table below shows the revised estimates for capital expenditure with the changes since the capital programme was agreed at the Budget in February 2016, and the expected financing arrangements of this capital expenditure. Additional grants and S106 contributions have been applied for 2016/17 due to slippage from 2015/16 and identification of funding against schemes.

Capital Expenditure by Service	2016/17 Original Budget £M	Current Budget £M	2016/17 Revised Forecast £M
General Fund	21.820	21.203	20.438
HRA	28.182	27.390	25.627
Total	**50.002**	**48.593**	**46.065**
Financed by:			
Capital grants & S106	0.757		2.905
Capital receipts & reserves	33.611		31.019
Revenue	5.796		5.796
Borrowing	9.838		6.345
Total financing	**50.002**		**46.065**
Borrowing need	**-**		**-**

7.4 The table below shows the CFR and the expected debt position over the period; termed the ‘Operational Boundary’. The changes to the forecast CFR are due to revision of the Capital Programme, and incorporation of the actual outturn position from 2015/16.

	2016/17 Original Estimate £M	2016/17 Revised Estimate £M
Prudential Indicator – Capital Financing Requirement		
CFR – General Fund	19.780	12.954
CFR – HRA	346.739	346.739
Total CFR	366.519	359.693
Net movement in CFR	**9.838**	**6.345**
Prudential Indicator – External Debt / the Operational Boundary		
Borrowing	366.519	366.519
Other long term liabilities	0.188	0.188
Total debt 31 March	**366.707**	**366.707**

7.5 Prudential Indicator for Borrowing Activity:

The key control over treasury activity is a prudential indicator 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 the next two financial years.

7.6 The table below demonstrates that, in line with this prudential indicator, the Council's forecast net borrowing does not exceed the CFR for 2016/17.

	2016/17 Original Estimate £M	2016/17 Revised Estimate £M
Gross borrowing	366.707	366.519
Plus other long term liabilities	0.188	0.188
Less investments	(35.408)	(57.030)
Net borrowing	331.487	309.677
CFR (year-end position)	366.519	359.693

Appendix 1 - Investment Portfolio as at 30 September 2016

Borrower	Deposit Type	Principal	Date Lent	Date Repayable	Interest Rate	Duration (Days)	Approved Duration	DBC Limit(M)
BlackRock	MMF	3,000,000	30/09/2016	03/10/2016	0.25%	3	100 days	7
Goldman Sachs	MMF	7,000,000	30/09/2016	03/10/2016	0.32%	3	100 days	7
Insight	MMF	7,000,000	30/09/2016	03/10/2016	0.35%	3	100 days	7
Coventry Building Society	Investment	1,000,000	12/04/2016	12/10/2016	0.60%	183	6 months	9
Close Brothers Ltd	Investment	4,000,000	29/04/2016	19/10/2016	0.67%	173	6 months	9
Debt Management Office	Investment	1,000,000	15/09/2016	25/10/2016	0.15%	40	60 months	n/a
BARCLAYS (DIRECT)	Investment	1,500,000	01/08/2016	04/11/2016	0.39%	95	6 months	9
Coventry Building Society	Investment	3,500,000	01/06/2016	22/11/2016	0.58%	174	6 months	9
Leeds Building Society	Investment	2,000,000	08/07/2016	25/11/2016	0.43%	140	6 months	9
Coventry Building Society	Investment	2,000,000	05/07/2016	04/01/2017	0.50%	183	6 months	9
Coventry Building Society	Investment	1,000,000	06/07/2016	06/01/2017	0.50%	184	6 months	9
Nationwide Building Society	Investment	1,000,000	15/07/2016	13/01/2017	0.49%	182	6 months	9
Santander UK plc	Investment	3,500,000	20/07/2016	16/01/2017	0.57%	180	6 months	9
Nationwide Building Society	Investment	1,000,000	21/07/2016	17/01/2017	0.48%	180	6 months	9
Nationwide Building Society	Investment	1,000,000	19/07/2016	18/01/2017	0.49%	183	6 months	9
Leeds Building Society	Investment	2,000,000	15/09/2016	19/01/2017	0.28%	126	6 months	9
Lloyds TSB Corporate Markets	Investment	4,000,000	17/08/2016	20/01/2017	0.60%	156	6 months	9
Lloyds TSB Corporate Markets	Investment	2,000,000	01/08/2016	31/01/2017	0.58%	183	6 months	9
BARCLAYS (DIRECT)	Investment	2,000,000	15/08/2016	15/02/2017	0.40%	184	6 months	9
Leeds Building Society	Investment	2,000,000	15/09/2016	17/02/2017	0.30%	155	6 months	9
Nationwide Building Society	Investment	1,000,000	31/08/2016	20/02/2017	0.40%	173	6 months	9
Coventry Building Society	Investment	1,500,000	31/08/2016	24/02/2017	0.37%	177	6 months	9
Leeds Building Society	Investment	2,000,000	13/09/2016	13/03/2017	0.34%	181	6 months	9
Santander UK plc	Investment	5,000,000	28/09/2016	20/03/2017	0.44%	173	6 months	9
Nationwide Building Society	Investment	5,000,000	27/09/2016	27/03/2017	0.43%	181	6 months	9
BARCLAYS (DIRECT)	Investment	2,000,000	30/09/2016	28/03/2017	0.42%	179	6 months	9
Royal Bank of Scotland plc	Investment	5,000,000	16/05/2016	16/05/2017	0.75%	365	12 months	12.5
Royal Bank of Scotland plc	Investment	2,500,000	02/08/2016	01/08/2017	0.70%	364	12 months	12.5
Royal Bank of Scotland plc	Investment	2,000,000	16/08/2016	15/08/2017	0.60%	364	12 months	12.5

Appendix 2 - Capita Approved Lending List – UK Banks and Financial Institutions

Country	Counterparty	Approved Duration	DBC Limit (M)
U.K	Abbey National Treasury Services plc	6 months	9
U.K	Bank of Scotland plc	6 months	9
U.K	Barclays Bank plc	6 months	9
U.K	Close Brothers Ltd	6 months	9
U.K	Goldman Sachs International Bank	6 months	9
U.K	HSBC Bank plc	12 months	10
U.K	Lloyds Bank plc	6 months	9
U.K	Santander UK plc	6 months	9
U.K	Standard Chartered Bank	100 days	7
U.K	Sumitomo Mitsui Banking Corporation Europe Ltd	6 months	9
U.K	UBS Ltd	6 months	9
U.K	Coventry BS	6 months	9
U.K	Leeds BS	6 months	9
U.K	Nationwide BS	6 months	9
U.K	Yorkshire BS	100 days	7
U.K	National Westminster Bank Plc	12 months	12.5
U.K	The Royal Bank of Scotland Plc	12 months	12.5