AUDIT COMMITTEE

Date of Meeting	Wednesday 16th March 2016
Report Subject	Treasury Management Update 2015/16
Report Author	Corporate Finance Manager

EXECUTIVE SUMMARY

The report provides an update on matters relating to the Council's Treasury Management Policy, Strategy and Practices 2015/16 to the end of February 2016.

RECOMMENDATIONS	
1	Members note the Treasury Management 2015/16 quarterly update.

REPORT DETAILS

1.00	EXPLAINING THE QUARTERLY UPDATE
1.01	The Council has nominated the Audit Committee to be responsible for ensuring effective scrutiny of Treasury Management Strategy and Policies. The Audit Committee has previously agreed to include Treasury Management as a standing item on each quarterly agenda to receive an update.
1.02	On 1st March 2013, the Council approved the Treasury Management Policy Statement 2013-2016 and Treasury Management Practices 2013-2016, following the recommendation of the Cabinet and consideration by the Audit Committee.
1.03	On 17th February 2015 the Council approved the Treasury Management Strategy 2015/16, following the recommendation of the Cabinet and consideration by the Audit Committee.

1.04	A statement setting out the Council's investments as at 29th February 2016 is attached at Appendix 1. The investment balance at this time was £40.5m, spread across 20 counterparties and the average investment rate was 0.57%.
1.05	There have been no changes to the Council's long term borrowing during the quarter. A schedule of outstanding loans as at 29th February is attached as Appendix 2, with total long-term borrowing remaining at £251.3m with a weighted average interest rate of 5.02%.
	Economic update
1.06	The global economy is facing a period of slower growth. China is importing less. Developing countries where extraction of raw materials is the primary industry are being impacted by lower global demand. More recently growth in the US has shown signs of slowing. As a result of the outlook for global growth being weak, share prices have fallen in the early part of 2016.
1.07	CPI inflation is currently very low at 0.3% (January 2016) due to oil and food prices. The anticipation is that the rate will remain below 1% for the duration of 2016 and start to rise toward the target of 2% either in 2017 or 2018.
1.08	Wage growth has also slowed with annual average earnings falling to 2% in the last quarter of 2015. Low inflation is likely to influence future wage settlements, with the projection for 2016 being lower than 2015.
1.09	UK economic growth was resilient in 2015 at 2.2%, albeit lower than 2014. Growth is reliant on consumer spending on the back of real wage and disposable income growth. Household spending is seen as the key determinant of growth in 2016, as growth in the manufacturing, services and construction industries all remain weak.
1.10	Arlingclose Ltd, the Council's treasury management advisors have pushed back their projection for the first rise in interest rates to the second quarter of 2018, from the third quarter of 2017. Stating the lack of inflationary pressures in 2016 and a lower growth profile than expected as the reasons.
1.11	The impact for the Council will be a lower return on investments and slightly lower than forecast cost associated with new borrowing. The figures are currently being worked through and will be reported in the revenue budget monitoring report.
1.12	The EU referendum in June and the uncertainty that it brings is already having an impact on the value of sterling and on financial markets. There is concern that there could be an impact on the wider economy, with reduced business investment and consumer confidence leading to a loss in economic momentum.
	Counterparty update
1.13	Following recent advice from Arlingclose Ltd the Council has suspended a bank from its counterparty list. The credit rating of the bank has been on review for downgrade by the credit rating agencies. It has very recently been downgraded, however its rating remains above the Council's threshold for investments. Arlingclose are taking a very cautious approach having

	considered the creditworthiness from other market data available including Credit Default Swaps, recently published preliminary results for financial year end 31st December 2015 and the revised risk from bail-in in the unlikely event of failure.
1.14	The Council has an investment of £1m with the bank which is due to mature on 10th June 2016. Having considered all of the risks the advice from Arlingclose Ltd is not to make any **new** investments with the affected counterparty, however **not** to break or sell any existing investments.

2.00	**RESOURCE IMPLICATIONS**
2.01	Financial implications set out in the report; no other resource implications directly as a result of this report.

3.00	**CONSULTATIONS REQUIRED / CARRIED OUT**
3.01	Arlingclose Ltd, being the Council's treasury management advisors.

4.00	**RISK MANAGEMENT**
4.01	Risk Management directly addressed within the report.

5.00	**APPENDICES**
5.01	1. Investment Portfolio as at 29th February 2016 2. Borrowing Portfolio as at 29th February 2016

6.00	**LIST OF ACCESSIBLE BACKGROUND DOCUMENTS**
6.01	**Contact Officer:** Liz Thomas – Technical Finance Manager **Telephone:** 01352 702289 **E-mail:** liz.thomas@flintshire.gov.uk

7.00	**GLOSSARY OF TERMS**
7.01	**Bank Rate:** The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate". **Basis Point:** A unit of measure used in finance to describe the percentage change in the value or rate of a financial instrument. One basis point is equivalent to 0.01% (1/100th of a percent). In most cases, it refers to changes in interest rates and bond yields. For example, if interest rates rise by 25 basis points, it means that rates have risen by 0.25% percentage points.

Bond: A certificate of debt issued by a company, government, or other institution. The bond holder receives interest at a rate stated at the time of issue of the bond. The price of a bond may vary during its life.

Capital Expenditure: Expenditure on the acquisition, creation or enhancement of capital assets.

Capital Financing Requirement (CFR): The Council's underlying need to borrow for capital purposes representing the cumulative capital expenditure of the local authority that has not been financed.

Credit Default Swaps: Similar to an insurance policy against a credit default.

Certificates of Deposits (CD's): A savings certificate entitling the bearer to receive interest. A CD bears a maturity date, a specified fixed interest rate and can be issued in any denomination. CDs are generally issued by commercial banks. The term of a CD generally ranges from one month to five years.

Cost of Carry: The "cost of carry" is the difference between what is paid to borrow compared to the interest which could be earned. For example, if one takes out borrowing at 5% and invests the money at 1.5%, there is a cost of carry of 3.5%.

Consumer Price Index (CPI): The UK's main measure of inflation (along with Retail Price Index or 'RPI') The Monetary Policy Committee of the Bank of England set the Bank Rate in order to try and keep CPI at or close to the target set by the Government. The calculation of CPI includes many items of normal household expenditure but excludes some items such as mortgage interest payments and Council Tax.

Credit Rating: Formal opinion by a registered rating agency of a counterparty's future ability to meet its financial liabilities; these are opinions only and not guarantees.

Corporate Bonds: Corporate bonds are bonds issued by companies. The term is often used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies.

Counterparty List: List of approved financial institutions with which the Council can place investments.

Debt Management Office (DMO): The DMO is an Executive Agency of Her Majesty's Treasury and provides direct access for local authorities into a government deposit facility known as the Debt Management Account Deposit Facility (DMADF). All deposits are guaranteed by HM Government and therefore have the equivalent of a sovereign credit rating.

Federal Reserve: The US central bank, the equivalent of the Bank of England. (Often referred to as "the Fed").

	Financial Instruments: Financial instruments are tradable assets of any kind. They can be cash, evidence of an ownership interest in an entity, or a contractual right to receive or deliver cash or another financial instrument **Gilts:** Gilts are bonds issued by the UK Government. They take their name from 'gilt-edged'. They are deemed to be very secure as the investor expects to receive the full face value of the bond to be repaid on maturity. **LIBID:** The London Interbank Bid Rate (LIBID) is the rate bid by banks on Eurocurrency deposits (i.e. the rate at which a bank is willing to borrow from other banks). **LIBOR:** The London Interbank Offered Rate (LIBOR) is the rate of interest that banks charge to lend money to each other. The British Bankers' Association (BBA) work with a small group of large banks to set the LIBOR rate each day. The wholesale markets allow banks who need money to borrow from those with surplus amounts. The banks with surplus amounts of money are keen to lend so that they can generate interest which it would not otherwise receive. **LOBO:** Stands for Lender Option Borrower Option. The underlying loan facility is typically very long-term - for example 40 to 60 years - and the interest rate is fixed. However, in the LOBO facility the lender has the option to call on the facilities at pre-determined future dates. On these call dates, the lender can propose or impose a new fixed rate for the remaining term of the facility and the borrower has the 'option' to either accept the new imposed fixed rate or repay the loan facility. **IFRS**: International Financial Reporting Standards. **Maturity:** The date when an investment or borrowing is repaid. **Maturity Structure / Profile:** A table or graph showing the amount (or percentage) of debt or investments maturing over a time period. **Monetary Policy Committee (MPC):** Government Body that sets the Bank Rate. Its primary target is to keep inflation within 1% of a central target of 2%. Its secondary target is to support the Government in maintaining high and stable levels of growth and employment. **Money Market Funds (MMF**): Pooled funds which invest in a range of short term assets providing high credit quality and high liquidity. **Minimum Revenue Provision (MRP**): An annual provision that the Council is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets. **Non Specified Investment**: Investments which fall outside the WG Guidance for Specified investments (below). **Operational Boundary:** This linked directly to the Council's estimates of the CFR and estimates of other day to day cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting

the most likely prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

Premiums and Discounts: In the context of local authority borrowing,
(a) the premium is the penalty arising when a loan is redeemed prior to its maturity date and
(b) the discount is the gain arising when a loan is redeemed prior to its maturity date.

Prudential Code: Developed by CIPFA and introduced in April 2004 as a professional code of practice to support local authority capital investment planning within a clear, affordable, prudent and sustainable framework and in accordance with good professional practice.

Prudential Indicators: Indicators determined by the local authority to define its capital expenditure and asset management framework. They are designed to support and record local decision making in a manner that is publicly accountable; they are not intended to be comparative performance indicators

Public Works Loans Board (PWLB): The PWLB is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.

Quantitative Easing (QE): In relation to the UK, it is the process used by the Bank of England to directly increase the quantity of money in the economy. It does not involve printing more banknotes. Instead, the Bank buys assets from private sector institutions – that could be insurance companies, pension funds, banks or non-financial firms – and credits the seller’s bank account. So the seller has more money in their bank account, while their bank holds a corresponding claim against the Bank of England (known as reserves). The end result is more money out in the wider economy.

Revenue Expenditure: Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges.

Retail Price Index (RPI): A monthly index demonstrating the movement in the cost of living as it tracks the prices of goods and services including mortgage interest and rent.

Term Deposits: Deposits of cash with terms attached relating to maturity and rate of return (Interest).

Specified Investments: Term used in the Welsh Assembly Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than one year. UK government, local authorities and bodies that have a high credit rating.

Supported Borrowing: Borrowing for which the costs are supported by the government or third party.

	Supranational Bonds: Instruments issued by supranational organisations created by governments through international treaties (often called multilateral development banks). The bonds carry an AAA rating in their own right. Examples of supranational organisations are the European Investment Bank, the International Bank for Reconstruction and Development. **Treasury Bills (T-Bills):** Treasury Bills are short term Government debt instruments and, just like temporary loans used by local authorities, are a means to manage cash flow. They are issued by the Debt Management Office and are an eligible sovereign instrument, meaning that they have an AAA-rating. **Treasury Management Code**: CIPFA's Code of Practice for Treasury Management in the Public Services, initially brought in 2003, subsequently updated in 2009 and 2011. **Treasury Management Practices (TMP):** Treasury Management Practices set out the manner in which the Council will seek to achieve its policies and objectives and prescribe how it will manage and control these activities. **Temporary Borrowing:** Borrowing to cover peaks and troughs of cash flow, not to fund capital spending. **Unsupported Borrowing**: Borrowing which is self-financed by the local authority. This is also sometimes referred to as Prudential Borrowing. **Yield:** The measure of the return on an investment instrument.