**Item 9**

Renfrewshire Council

**To:** **Finance and Resources Policy Board**

**On:** **11 November 2015**

**Report by:** **Director of Finance and Resources**

**Heading:** **Treasury Management Mid-year Review 2015-2016**

## 1. Summary

1.1 This mid-year report has been prepared in compliance with the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services Code of Practice (revised November 2009) which was adopted by Council on 3 March 2010. The report covers the following:

- an economic update for the first six months of 2015-2016;
- a review of the Treasury Management Strategy Statement 2015-2016, incorporating the annual investment strategy;
- a review of the Council's investment portfolio for 2015-2016;
- a review of the Council's borrowing strategy for 2015-2016; and
- a review of compliance with treasury management indicators for 2015-2016.

## 2. Recommendations

2.1 It is recommended that Members note the treasury management activity for the period 1 April 2015 to 9 October 2015.

## 3. Economic update

3.1 **External economic review for the period April to October 2015**
The Council's treasury advisers have provided the Council with a review of the economy over the first half of 2015-2016 and this is outlined below for members' reference.

3.2 UK GDP growth rates in 2013 of 2.2% and 2.9% in 2014 were the strongest growth rates of any G7 country. Quarter 1 of 2015 was weak at +0.4%, although there was a recovery in quarter 2 to +0.7% (+2.4% y/y). Growth is expected to weaken marginally to about +0.5% in quarter 3 as the economy faces pressures for exporters from the appreciation of Sterling against the Euro. Weak growth in the EU, China and emerging markets along with the continuing dampening effect of the UK Government's austerity programme are all likely to continue to hold back growth.

3.3 Despite these pressures, the Bank of England August Inflation Report had included a forecast for growth to remain around 2.4 – 2.8% over the next three years, driven mainly by strong consumer demand as the squeeze on the disposable incomes of consumers has been reversed by a recovery in wage inflation at the same time that CPI inflation has fallen to, or near to, zero over the last quarter. Investment expenditure is also expected to support growth. However, since then worldwide economic statistics have been distinctly weak and it is highly likely that these forecasts will be cut in the next Inflation Report out in November.

3.4 The August Bank of England Inflation Report forecast was notably subdued with inflation barely getting back up to the 2% target within the 2-3 year time horizon. However, with the price of oil taking a fresh downward direction and Iran expected to soon rejoin the world oil market after the impending lifting of sanctions, there could be several more months of low inflation still to come, especially as world commodity prices have generally been depressed by the Chinese economic downturn.

3.5 There are therefore considerable risks around whether inflation will rise in the near future as strongly as previously expected. This will make it more difficult for the central banks of both the US and the UK to raise interest rates as soon as had previously been expected, especially given the recent major concerns around the slowdown in Chinese growth, the knock on impact on the earnings of emerging countries from falling oil and commodity prices, and the volatility we have seen in equity and bond markets in 2015. This could potentially spill over to impact countries real economies rather than just financial markets.

3.6 **Economic outlook for the remainder of 2015-2016**
The overall balance of risks to economic recovery in the UK is currently evenly balanced. There remains uncertainty in economic forecasts due to a wide range of factors in a number of key areas.

Risks which would influence an increase in Public Works Loan Board (PWLB) borrowing rates include for example:

- Uncertainty around the outcome of a UK referendum on EU membership.
- The European Central Bank disappointing financial markets with a programme of quantitative easing which proves insufficient to significantly stimulate growth in the eurozone.
- The commencement by the US Federal Reserve of increases in the federal funds rate causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.
- UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

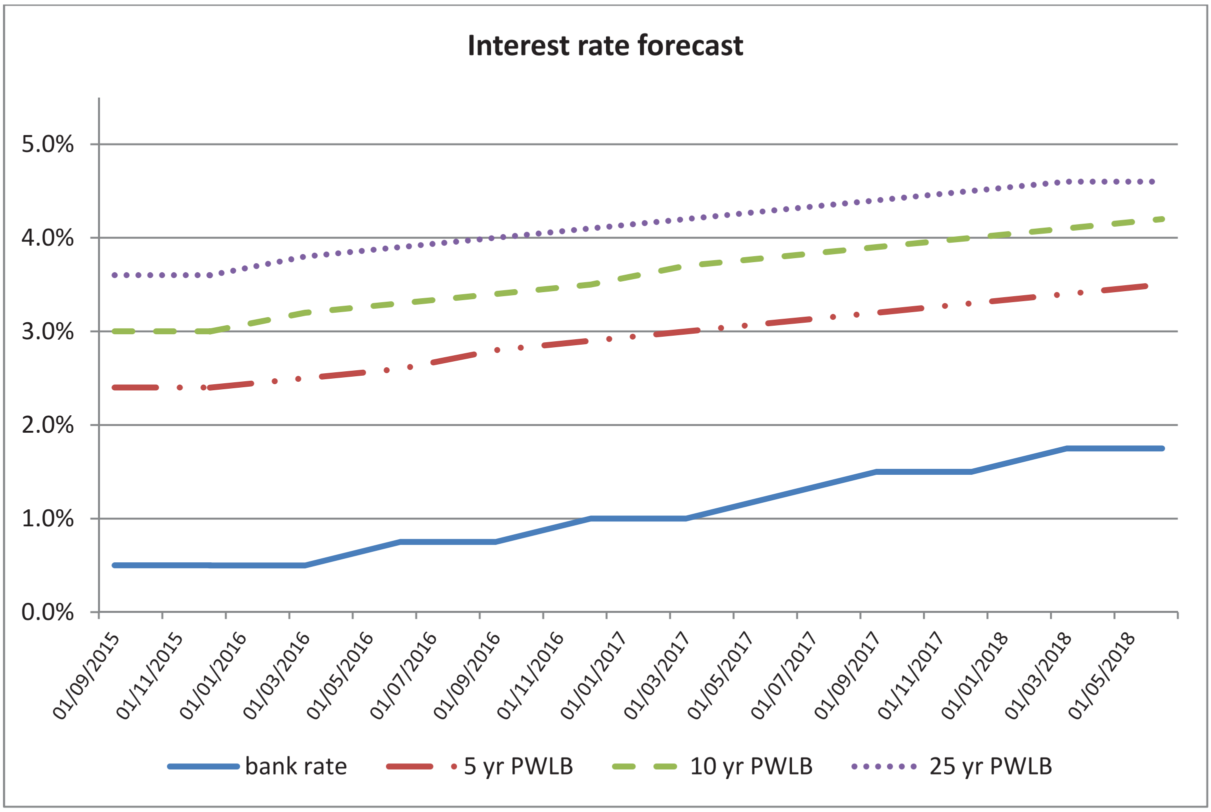
Risks which would influence a decrease in PWLB borrowing rates currently include for example:

- Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.
- UK economic growth turns significantly weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU, US and China.
- A resurgence of the eurozone sovereign debt crisis.

3.7 **Interest rate forecast**

Market forecasts indicate the Bank Rate is now not expected to start to increase until quarter 2 of 2016. As CPI inflation is now likely to be at or near zero for most of 2015, it is difficult for the MPC to make a start on increasing the Bank Rate when the Inflation Report forecast is also notably subdued with inflation barely getting back up to the 2% target within the 2-3 year time horizon. Despite average weekly earnings increasing to 2.9% year on year in the three months ending in July, this is unlikely to provide sufficient evidence for the MPC to take action to raise Bank Rate soon. The significant appreciation of Sterling against the Euro in 2015 has also acted as a dampening to UK growth while sharp volatility in financial markets since the Inflation Report has depressed equity prices, raised bond prices and lowered bond yields (and PWLB rates).

3.8 The Governor of the Bank of England, Mark Carney, has repeatedly stated that increases in Bank Rate will be slow and gradual. The MPC is concerned about the impact of increases on many heavily indebted consumers, especially when average disposable income is only just starting to recover as a result of recent increases in the rate of wage inflation, though some consumers will not have seen that benefit come through for them.




## 4 Review of the Treasury Management Strategy Statement 2015-2016 (incorporating annual investment strategy) as at 9 October 2015

4.1 The Treasury Management Strategy Statement for 2015-2016 was approved by Council on 12 February 2015. The Council's annual investment strategy, which is incorporated in the Treasury Management Strategy Statement, sets out the Council's investment priorities as follows:

- the security of capital and
- the liquidity of its investments.

4.2 The Council also aims to achieve the optimum returns on its investments commensurate with the proper levels of security and liquidity.

4.3 Investments and borrowing during the first six months of the year have been in line with the strategy and there have been no changes to the policies set out in the Treasury Management Strategy Statement 2015-2016. The details in this report update the position in light of the updated economic position and budgetary changes already approved.

## 5 Review of borrowing and investments over the period 1 April 2015 to 9 October 2015

5.1 The Council's net borrowing position as at 9 October 2015 is shown in Appendix 1.

5.2 During the period 1 April 2015 to 9 October 2015 the Council's total external borrowings decreased by £3.933 million to £221.868 million, mainly due to the scheduled repayments of PWLB debt. However, short-term borrowings have increased in this period by £1.739 million as a result of a net increase in deposits temporarily held for Renfrewshire Leisure Limited, who invest in the Council's loans fund.

5.3 During the period 1 April 2015 to 9 October 2015, temporary investments have increased by £37.870 million to £93.720 million. The increase in investments is after financing the £5.672 million of debt repayment and reflects:

- the re-profiling of elements of the current capital programme;
- the "front-loading" (that is, more income being received in the early part of the year) of revenue support grant income and non-domestic rates pool receipts.

5.4 The Director of Finance and Resources confirms that, during the period 1 April 2015 to 9 October 2015, the approved limits set out within the annual investment strategy sections of the Treasury Management Strategy Statement 2015-2016 were complied with. The Council only invested with institutions listed in the Council's approved lending list. Similarly, only permitted investment vehicles were used, mainly call accounts, fixed term deposits and money market funds.

5.5 In accordance with CIPFA's Treasury Management in the Public Services Code of Practice, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite.

5.6 The table below shows the average interest rate achieved by the Council on its temporary investments during the period 1 April 2015 to 9 October 2015. The table also shows for comparison the benchmark comparator, which is the average 7-day LIBID rate (uncompounded) sourced from Capita Treasury Services Limited. (The 7-day LIBID rate means the London Interbank Bid Rate, being the rate at which a bank is willing to borrow from other banks, for borrowings of a maturity of seven days.)

| Interest rates achieved on investments | Average value of investments | Actual rate of return | Benchmark return |
|---|---|---|---|
| Internally managed investments | £74.629m | 0.619% | 0.362% |

5.7 **Debt rescheduling**

Debt rescheduling opportunities have been limited in the current economic climate and it is not anticipated that this is likely to change over the short to medium term. However, in conjunction with the Council's treasury advisors, the service will remain alert to any opportunities which may arise.

## 6 Review of compliance with treasury management indicators for 2015-2016

6.1 During the period 1 April 2015 to 9 October 2015 the Council complied with the approved treasury management indicators as set out in the Treasury Management Strategy Statement 2015-2016. These indicators relate to:

- interest rate exposures: the upper limit on the proportion of investments which are exposed to fixed interest rates and the upper limit on the proportion of investments which are exposed to variable interest rates;
- the maturity structure of borrowing: the lower and upper limits on the proportion of investments which fall into each maturity band.

6.2 In addition to the treasury management indicators described at 6.1, there are two *prudential* indicators (as set out in the Prudential Framework for Capital Finance 2015-2018 and Treasury Management Strategy Statement 2015-2016, approved by Council on 12 February 2015) which are of particular relevance to the Council's treasury management strategy:

- operational boundary for external debt;
- authorised limit for external debt.

6.3 During the period 1 April 2015 to 9 October 2015 the Council operated within the operational boundary for external debt, and within the authorised limit for external debt. These indicators, along with the Council's *actual* external debt, are shown in Appendix 2.

**Implications of the Report**

1. **Financial** – As described in the report. The Treasury Management Strategy Statement and treasury management indicators assist in providing assurance that the Council's treasury management activities and longer term plans are affordable, prudent and sustainable.

2. **HR & Organisational Development** – none

3. **Community Planning** – none

4. **Legal** – none

5. **Property/Assets** – none

6. **Information Technology** – none

7. **Equality & Human Rights** – Recommendations contained within this report have been assessed in relation to their impact on equalities and human rights. No negative impacts on equality groups or potential for infringement of individuals' human rights have been identified arising from the recommendations contained in the report because it is for noting only. If required following implementation, the actual impact of the recommendations and the mitigating actions will be reviewed and monitored, and the results of the assessment will be published on the Council's website.

8. **Health & Safety** – none

9. **Procurement** – none

10. **Risk** – The Treasury Management Strategy Statement and treasury management indicators provide a framework to take forward the Council's treasury activities in the context of the effective control of the risks associated with those activities and the pursuit of optimum performance consistent with those risks. This mid-year review report demonstrates that the treasury management activities carried out during the period 1 April 2015 to 9 October 2015 have been consistent with the Treasury Management Strategy Statement 2015-2016 and have complied with the treasury management indicators set out in the Strategy Statement

11. **Privacy Impact** – none

---

**List of Background Papers**

None

**Author**: Richard Conway – 0141 618 7377

# Appendix 1

**Borrowing and investment position as at 9 October 2015**

| | balance at 01-Apr-15 | new borrowing in 2015-2016 | principal repayments | debt restructuring | net cash movements | balance at 09-Oct-15 |
|---|---|---|---|---|---|---|
| **Long term borrowings** | | | | | | |
| PWLB - fixed | 172,640,995.00 | - | (5,672,277.99) | - | - | 166,968,717.01 |
| PWLB - variable | - | - | - | - | - | - |
| Market loans | 52,916,000.00 | - | - | - | - | 52,916,000.00 |
| | 225,556,995.00 | - | (5,672,277.99) | - | - | 219,884,717.01 |
| **Short term borrowings** | | | | | | |
| Temporary loans | - | - | - | - | - | - |
| Renfrewshire Leisure Ltd | 243,613.45 | | 1,739,494.42 | - | - | 1,983,107.87 |
| | 243,613.45 | - | 1,739,494.42 | - | - | 1,983,107.87 |
| **Total external borrowings** | 225,800,608.45 | - | (3,932,783.57) | - | - | 221,867,824.88 |
| **Investments** | | | | | | |
| Fixed term deposits | 24,650,000.00 | - | - | - | 29,070,000.00 | 53,720,000.00 |
| Notice accounts | 5,000,000.00 | - | - | - | 1,000,000.00 | 6,000,000.00 |
| Call accounts | 17,000,000.00 | - | - | - | 1,000,000.00 | 18,000,000.00 |
| Money market funds | 9,200,000.00 | - | - | - | 6,800,000.00 | 16,000,000.00 |
| **Total investments** | 55,850,000.00 | - | - | - | 37,870,000.00 | 93,720,000.00 |
| **Net borrowing** | 169,950,608.45 | - | (3,932,783.57) | - | 37,870,000.00 | 128,147,824.88 |

## Appendix 2

### Treasury Management Indicators as at 9 October 2015

| | 2015-2016 estimate | 2015-2016 probable | 2016-2017 estimate | 2017-2018 estimate |
|---|---|---|---|---|
| **Authorised limit for external debt** | £383m | £377m | £388m | £397m |
| **Operational boundary for external debt** | £368m | £362m | £372m | £383m |
| **Actual external debt at 9 October 2015** | n/a | £307m | n/a | n/a |
| **Upper limit for fixed interest rate exposure (borrowing)** expressed as percentage of total net outstanding principal | 100% | n/a | 100% | 100% |
| **Upper limit for variable interest rate exposure (borrowing)** expressed as percentage of total net outstanding principal | 25% | n/a | 25% | 25% |

-

| | new borrowing in 2015-2016 | | total of all borrowing | |
|---|---|---|---|---|
| | value | maturity structure | upper limit | actual at 9 Oct 2015 |
| **Maturity structure of fixed rate borrowing** | | | | |
| under 12 months | 0 | 0% | 15% | 0.47% |
| 12 months and within 24 months | 0 | 0% | 15% | 5.24% |
| 24 months and within 5 years | 0 | 0% | 45% | 8.21% |
| 5 years and within 10 years | 0 | 0% | 50% | 4.45% |
| 10 years and above | 0 | 0% | 100% | 81.63% |