Cherwell District Council

Accounts, Audit and Risk Committee

3 December 2014

Q2 Treasury Management Report and Draft Treasury Management Strategy 2015/16

Report of the Head of Finance and Procurement

This report is public

Purpose of report

To receive information on treasury management performance and compliance with treasury management policy for 2014-15 for Quarter 2 including an update for position as at 31 October 2014 as required by the Treasury Management Code of Practice.

To provide a review of the draft Treasury Management Strategy 2015-16

1.0 Recommendations

The meeting is recommended:

1.1 To note the contents of the Quarter 2 (Q2) Treasury Report

1.2 To note the draft Treasury Management Strategy 2015/16

2.0 Introduction

2.1 As part of our investment strategy and governance arrangements this committee considers the investment performance to date and our compliance with counterparties being used.

2.2 The Code of Practice on Treasury Management approved by the Chartered Institute of Public Finance and Accountancy (CIPFA) and adopted in full by the Council in 2004, requires that a Treasury Management Strategy is produced prior to the beginning of the financial year to which it relates. The Treasury Management Strategy is the cornerstone of proper treasury management, and is central to the operation, management reporting and performance assessment. An updated Strategy for Cherwell District Council was approved at a Special Council meeting on 7 July 2014.

2.3 The Council re-appointed Sector Treasury Services Limited (now Capita Treasury Solutions Limited and branded as Capita Asset Services – Treasury Solutions) as its Treasury Management advisor in January 2013. The highest standard of stewardship of public funds remains of the utmost importance to the Council. This document details the Council's management of investments and treasury management activities during the first 6 months of 2014-15.

3.0 Report Details

2014-15 Performance

3.1 As at the end of September the Council had £58.12m managed in-house (including the balance of the Eco Town funds but excluding the outstanding Icelandic deposit) which fluctuates during the year. The Council regularly reviews each of these funds in light of the current economic climate, reducing balances in investments planned to fund the Capital Programme, and the need to contribute to efficiency savings.

Update on Cherwell's Treasury Performance

3.2 An updated Treasury Management Strategy for 2014-15, which includes the Annual Investment Strategy, was approved at Special Council on 7 July 2014. It sets out the Council's investment priorities as being: Security of Capital; Liquidity; and Yield.

3.3 The Council will also aim to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term to cover short term cash flow needs. However, the Council also seeks out value available in significantly higher rates in periods up to 12 months with highly credit rated financial institutions. The Council uses Sector's suggested creditworthiness approach, including sovereign credit rating and Credit Default Swap (CDS) overlay information provided by Sector (this applies in particular to nationalised and semi nationalised UK banks).

3.4 During the quarter ended 30th September, Capita Asset Services highlighted: -

- After strong UK GDP quarterly growth of 0.7%, 0.8% and 0.7% in quarters 2, 3 and 4 respectively in 2013, (2013 annual rate 2.7%), and 0.7% in Q1 and 0.9% in Q2 2014 (annual rate 3.2% in Q2), it appears very likely that strong growth will continue through 2014 and into 2015 as forward surveys for the services and construction sectors, are very encouraging and business investment is also strongly recovering. The manufacturing sector has also been encouraging though the latest figures indicate a weakening in the future trend rate of growth. However, for this recovery to become more balanced and sustainable in the longer term, the recovery needs to move away from dependence on consumer expenditure and the housing market to exporting, and particularly of manufactured goods, both of which need to substantially improve on their recent lacklustre performance.

  This overall strong growth has resulted in unemployment falling much faster through the initial threshold of 7%, set by the Monetary Policy Committee (MPC) last August, before it said it would consider any increases in Bank Rate. The MPC has, therefore, subsequently broadened its forward guidance by adopting five qualitative principles and looking at a much wider range of about eighteen indicators in order to form a view on how much slack there is in the economy and how quickly slack is being used up. The MPC is particularly concerned that the current squeeze on the disposable incomes of consumers should be reversed by wage inflation rising back above the level of inflation in order to ensure that the recovery will be sustainable. There also needs to be a major improvement in labour productivity, which has languished at dismal levels since 2008, to support increases in pay rates. Most economic forecasters are expecting growth to peak in 2014 and then to ease off a little, though still remaining strong, in 2015 and 2016. Unemployment is therefore expected to keep on its downward trend and this is likely to eventually feed through into a return to significant increases in pay rates at some point during the next three years. However, just how much those future increases in pay rates will counteract the depressive effect of increases in Bank Rate on consumer confidence, the rate of growth in consumer expenditure and the buoyancy of the housing market, are areas that will need to be kept under regular review.

- Also encouraging has been the sharp fall in inflation (CPI), reaching 1.5% in July, the lowest rate since 2009. Forward indications are that inflation is likely to fall further in 2014 to possibly 1%. The return to strong growth has also helped lower forecasts for the increase in Government debt by £73bn over the next five years, as announced in the Autumn Statement, and by an additional £24bn, as announced in the March 2014 Budget - which also forecast a return to a significant budget surplus, (of £5bn), in 2018-19. However, monthly public sector deficit figures have disappointed so far this year.
- In September, the U.S. Federal Reserve continued with its monthly $10bn reductions in asset purchases, which started in December 2014. Asset purchases have now fallen from $85bn to $15bn and are expected to stop in October 2014, providing strong economic growth continues. First quarter GDP figures were depressed by exceptionally bad winter weather, but quarter 2 rebounded strongly to 4.6%.
- The Eurozone is facing an increasing threat from deflation. In September, the inflation rate fell further, to reach 0.3%. However, this is an average for all EZ countries and includes some countries with negative rates of inflation. Accordingly, the ECB did take some rather limited action in June and September to loosen monetary policy in order to promote growth.

3.5 Investment rates available in the market have been broadly stable during the quarter and have continued at historically low levels as a result of the ultra-low Bank Rate and other extraordinary measures such as the Funding for Lending Scheme.
The annualised average level of funds available for investment purposes up to September 2014 was £61.361m. These funds were available on a temporary basis, and the level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme and ECO Bicester.

3.6 It is worth noting that the revenue budget for 2014-15 has been prepared utilising only £49,190 of investment income; however, total Investment income within 2014-15 is budgeted as £320,000. The balance above the £49,190 budget will be used to replenish reserves after transferring interest received in respect of Eco Town funds to the Eco Town reserve.

Investment performance for quarter ended 30 September 2014 was:

Fund	**Funds invested 30th September 2014**	**Interest Budget**	**Actual Interest**	**Variance**	**Rate of return %**
In House	£58,120,000	£160,000	£194,721	£34,721	0.62
Total	**£58,120,000**	**£160,000**	**£194,721**	**£34,721**	

**Rate of Return is calculated on an annualised basis*

3.7 At this point in the year we are currently projecting to be on target. The variance shown above for in-house investments has arisen through the timing of actual interest due and received.

3.8 The performance as at the **31 October** as follows.

Fund	Amount at 31st October 2014	Interest Budget	Actual Interest	Variance	Rate of return %
In House	£59,630,000	£186,667	£228,808	£42,141	0.62
Total	**£59,630,000**	**£186,667**	**£228,808**	**£42,141**	

3.9 For Quarter 2, Appendix 1 shows the counterparties that the Council has invested with at the end of September

Draft Treasury Management Strategy 2015-16

3.10 The proposed draft strategy for 2014-15 is based upon the views of the Council's Treasury Management Team. This is informed by market forecasts provided by the Council's treasury advisor, Capita Asset Services.

3.11 In consultation with Capita Asset Services and with full reference to the CIPFA Code of Practice, the Council has reviewed its risk appetite and associated priorities in relation to security, liquidity and yield in respect of returns from various financial instruments.

3.12 The draft strategy meets the requirements included within the CLG's Guidance on local government investments.

Icelandic Investments

3.13 There is currently no further update in respect of funds remaining within Iceland. As reported previously, out of the £6.5m original capital investment £5.7m has been returned to the Council. The remaining capital balance of £729,669 along with associated interest relating to the investment is still held within Iceland and is accruing interest on an annual basis.

4.0 Conclusion and Reasons for Recommendations

4.1 This report details the Treasury Performance for the Council for the quarter ended 30 September 2014

5.0 Consultation

None

6.0 Alternative Options and Reasons for Rejection

6.1 The following alternative options have been identified and rejected for the reasons as set out below.

Option 1: To request further information on the performance reported.

7.0 Implications

Financial and Resource Implications

7.1 There are no financial implications arising directly from any outcome of this report.

Comments checked by:
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Legal Implications

7.2 Presentation of this report is in line with the CIPFA Code of Practice.

Comments checked by:
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Risk Management Implications

7.3 It is essential that this report is considered by AARC as it demonstrates that the risk of not complying with the Council's Treasury Management Policy has been avoided

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8.0 Decision Information

Wards Affected

All wards are affected

Links to Corporate Plan and Policy Framework

All corporate plan themes.

Lead Councillor

None

Document Information

Appendix No	Title
Appendix 1 Appendix 2	Treasury Investments Q2 Treasury Management Strategy 2015-16
Background Papers	
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