Appendices
2

NORTHAMPTON
BOROUGH COUNCIL

CABINET REPORT

Report Title	TREASURY MANAGEMENT OUTTURN 2014-15

AGENDA STATUS: **PUBLIC**

Cabinet Meeting Date:	9 September 2015
Key Decision:	NO
Within Policy:	YES
Policy Document:	NO
Directorate:	LGSS
Accountable Cabinet Member:	Mike Hallam
Ward(s)	Not Applicable

1. Purpose

1.1 To inform Cabinet of the Council's performance in relation to its borrowing and investment strategy for 2014-15, and provide an update of the same in respect of the first quarter of 2015-16.

2. Recommendations

2.1 That Cabinet recommend to Council that they note the Council's treasury management performance for 2014-15 (outturn), and updated treasury management data for quarter 1 of 2015-16.

3. Issues and Choices

3.1 CIPFA Code of Practice on Treasury Management in the Public Services

3.1.1 The Council has adopted the CIPFA Code of Practice on Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes ("the Treasury Management Code of Practice").

3.2 Issues

Summary of Key Headlines

3.2.1 The main headlines for the period are:

- The Council continued to make use of internal borrowing to fund its capital expenditure programme, generating savings in the revenue budget. This benefits the Council's revenue budget position as the costs of external borrowing are avoided, at least until such time as the Council's cash position or interest rate conditions change and there are drivers to go to the external market. See paragraph 3.2.24

- In house investment returns received on cash balances compared favourably to the benchmarks. A return of 0.66% was achieved compared to the 7 day LIBID benchmarks of 0.35%. In respect of local authority benchmarks the NBC performance has been in line with or above the comparator group averages throughout the year. See paragraphs 3.2.30 to 3.2.36.

- The debt financing budget outturn was £477k under budget, due to a number of factors, of which the most important was that the Council had significantly higher levels of cash balances throughout the year than budgeted. See paragraphs 3.2.46 to 3.2.47

- The Council has operated throughout the year within the Treasury and Prudential Indicators set out in the Council's Treasury Management Strategy Statement (TMSS) and in compliance with the Council's Treasury Management Practices. See paragraph 3.2.51 to 3.2.53

- The borrowing position at the end of quarter 1 2015-16 was broadly unchanged from that as at 31 March 2015. See paragraph 3.2.25

- Investment balances during quarter 1 2015-16 averaged £79m, with a weighted average rate of interest of 0.72%. See paragraph 3.2.37

The Economic Environment

3.2.2 A detailed commentary for the quarter ending 30 June 2015 is provided in **Appendix 1** to advise Members of the latest economic position. This information has been provided by Capita Asset Services – Treasury Solutions (CAS Treasury Solutions), the Council's treasury management advisors.

3.2.3 The key economic messages are:

- The economic recovery slowed in the first quarter;
- Survey measures pointed to renewed vigour in Q2;
- Wage growth picked up as the labour market tightens;
- Deflation lasted only one month, but the outlook remain subdued;
- Another split vote on the MPC drew nearer, but a rate hike this year remained unlikely;
- The general election confirmed that the fiscal squeeze will re-intensify next year;
- The possibility of a "Grexit" became greater

Risk implications of decisions taken and transactions executed

3.2.4 The Treasury Management Code of Practice identifies eight main treasury management risks. Definitions of these are included in the Council's Treasury Management Practices (TMPs) for 2014-15 approved by Council 24 February 2014. The management of these risks during 2014-15 is covered in the following paragraphs.

a) Credit and counterparty risk – This continued to be an area of considerable risk for all local authority investors, given the prevailing uncertain economic and banking environment. The Council managed this risk extremely closely during the year through strict adherence to its treasury management policies and practices and a tightly controlled counterparty list that took into account a range of relevant factors including sovereign rating, credit ratings, inclusion in the UK banking system support package and credit default swap spreads. The advice of the Council's treasury management advisors was also an underlying feature. None of the Council's counterparties failed to meet the contractual obligations of their treasury transactions with the Council during 2014-15.

b) Liquidity risk – This was managed effectively during 2014-15 through pro-active management of the Council's cashflow, including the choice of suitable investment values and maturity dates and the maintenance of sufficient levels of liquid cash in money market funds and deposit accounts. The Council also maintained its access to overdraft facilities and temporary borrowing facilities as a contingency for use in exceptional circumstances. The Council undertook no long or short-term borrowing to manage liquidity during 2014-15.

c) Interest rate risk - The Council's upper limits for fixed and variable interest rate exposures in respect of investments, borrowing and net external debt are managed as treasury indicators. These are reported at **Appendix 2**. The indicators were not breached during 2014-15.

d) Exchange rate risk - The Council has a policy of only entering into loans and investments that are settled in £ sterling, and has no treasury management exposure to this category of risk.

e) Refinancing risk – The Council did not refinance any of its debt during 2014-15 and was therefore not exposed to this category of risk during the year.

f) Legal and regulatory risk - The Council carried out its treasury management activities for 2014-15 within the current legal and regulatory framework. LGSS officers responsible for strategic and operational treasury management decisions are required to keep abreast of new legislation and regulations impacting on the treasury management function, and have applied any changes as necessary. Legal and regulatory risks associated with other organisations with which the Council deals in its treasury management activities have been managed through counterparty risk management policies.

g) Fraud, error and corruption and contingency management – LGSS officers involved in treasury management are explicitly required to follow treasury management policies and procedures when making investment and borrowing decisions on behalf of the Council. All treasury activities must be carried out in strict accordance with the agreed systems and procedures in order to prevent opportunities for fraud, error and corruption. The measures in place to ensure this include a scheme of delegation and segregation of duties, internal audit of the treasury function, detailed procedure notes for dealing and other treasury functions, and emergency and contingency planning arrangements (including a business continuity plan for treasury management).

h) Market risk – Investments that may be subject to fluctuations in market value in some circumstances include certificates of deposit, gilts, bonds and money market funds.

   The Council has deposits placed in money market funds, whereby the underlying assets of the fund are subject to capital fluctuations as a result of interest rate risk and credit risk. However the structure of the fund minimises the movement of capital value due to the restrictions laid down by the credit rating agencies. The Council did not experience any fluctuations in the capital value of its money market funds in 2014-15.

   The Council purchased certificates of deposit in 2014-15. In the main these were held to maturity and were not subject to movement in capital value. Two certificates of deposit taken out in 2014-15 were sold prior to maturity in the first quarter of 2015-16, on the advice of the broker, to realise a capital gain.

   The Council did not invest in gilts or bonds during 2014-15.

Summary Portfolio Position

3.2.5 A snapshot of the Council's debt and investment position is shown in the table below:

	Actual as at 31 March 2014		TMSS 2014-15 31 March 15 Forecast (as agreed by Council Feb 2014)		Actual at 31 March 2015		Actual at 30 June 2015	
	£m	Rate %	£m	Rate %	£m	Rate %	£m	Rate %
Borrowing								
HRA	193.0	3.29%	193.0	3.29%	193.0	3.29%	193.0	3.29%
GF	23.0	5.53%	27.7	4.86%	15.1	3.22%	15.1	3.23%
GF - Third Party Loans	10.0	3.32%	39.3	4.75%	15.5	3.14%	15.5	3.14%
Total Borrowing	**226.0**	**3.56%**	**260.0**	**4.28%**	**223.6**	**3.28%**	**223.6**	**3.28%**
Investments	**73.0**	**0.61%**	**35.0**	**0.50**	**64.3**	**0.73%**	**79.9**	**0.75%**
Total Net Debt / Borrowing	**153.0**		**225.0**		**159.2**		**143.7**	
Third party loans	**10.0**		**39.3**		**16.9**		**17.2**	

3.2.6 The table shows the extent of which cash balances are used to finance capital expenditure. This benefits the Council's revenue budget position as the costs of external borrowing are avoided, at least until such time as the Council's cash position or interest rate conditions change and there are drivers to go to the external market.

3.2.7 Further analysis of borrowing and investments is covered in the following two sections.

Borrowing

3.2.8 The Council can take out loans in order to fund spending for its capital programme for the benefit of Northampton. The amount of new borrowing needed each year is determined by capital expenditure plans and projections of the Capital Financing Requirement (CFR), forecast reserves and current and projected economic conditions.

New loans and repayment of loans:

3.2.9 The table below shows the details of new loans raised and loans repaid during the year 2014-15. All borrowing activity relates to the General Fund.

3.2.10 Two LOBO loans with a total amortised value of £15.72m were repaid on maturity. These were at interest rates of 5.68% (£11.6m) and 7.03% (£4.12m).

The loans were re-financed using surplus cash resources, realising net savings of £829k in 2015-16.

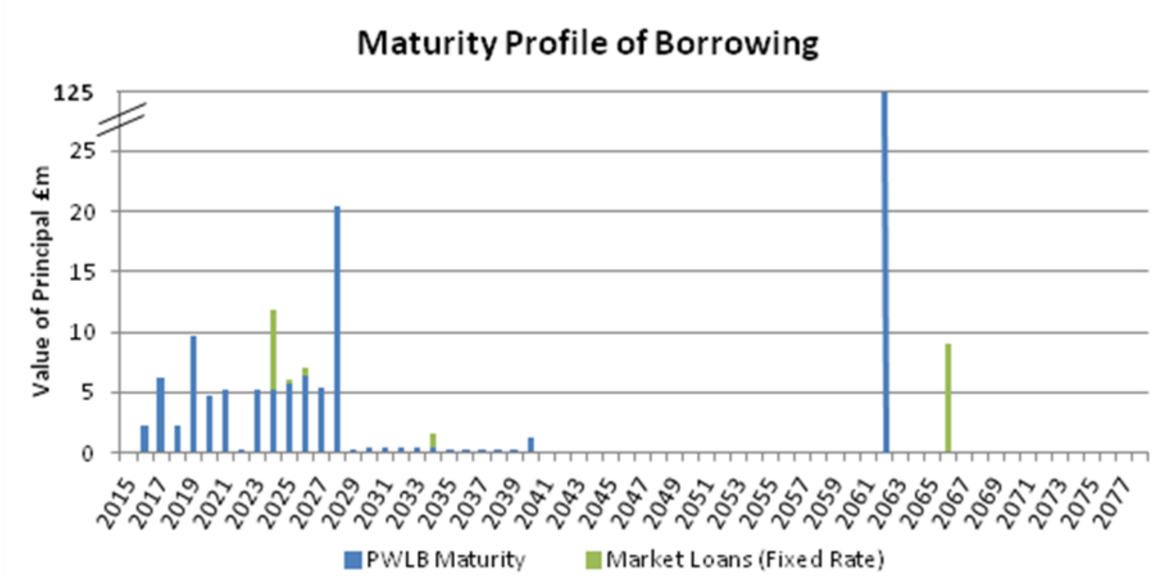
3.2.11 The Growing Places Fund (GPF) and Local Infrastructure Funding (LIF) are loans provided through government agencies to support the infrastructure schemes in the Enterprise Zone (EZ). The GPF loan, accessed through SEMLEP, is funding St Peters Way Roundabout/Black Lion Hill and the Cosworth site. The LIF loan, provided by the Homes and Communities Agency (HCA), is funding the St James Mill Road sub-station. Both provide bridge funding until such time as they can be repaid from the business rates uplift that will arise in the EZ.

3.2.12 Much of the remaining activity related to borrowing from the PWLB to fund loans to third parties, and repayment of annual amounts on EIP and annuity loans related to this borrowing.

Lender	Loan Type	Start Date	Maturity Date	£m	Interest Rate %	Duration (yrs)	Comments
Raised							
Public Works Loan Board	Maturity	17/04/2014	17/04/2019	1.52	2.54	5	To fund third party loan
Public Works Loan Board	Maturity	12/05/2014	12/05/2019	1.52	2.68	5	To fund third party loan
Public Works Loan Board	Maturity	19/08/2014	19/08/2019	1.50	2.58	5	To fund third party loan
Public Works Loan Board	Annuity	22/07/2014	22/07/2039	1.24	3.82	25	To fund third party loan
Growing Places Fund	Bespoke	01/09/2014	01/04/2022	1.04	1.74	8	To be repaid from business rates uplift. Repayment date is target repayment date
Growing Places Fund	Bespoke	23/10/2014	02/04/2022	2.46	1.74	7	
Growing Places Fund	Bespoke	13/01/2015	03/04/2022	0.13	1.74	7	
Growing Places Fund	Bespoke	14/01/2015	04/04/2022	3.01	1.74	7	
Local Infrastructure Funding	Bespoke	24/12/2014	31/03/2026	0.34	3.07	11	To be repaid from business rates uplift. Repayment date is final repayment date (some amounts are due for repayment earlier)
Local Infrastructure Funding	Bespoke	06/02/2015	31/03/2026	0.28	3.07	11	
Local Infrastructure Funding	Bespoke	27/02/2015	31/03/2026	0.26	3.07	11	
Local Infrastructure Funding	Bespoke	31/03/2015	31/03/2026	0.15	3.07	11	
Repaid							
Landesbank Hessen-Thuringen	LOBO	06/03/2000	06/03/2015	4.12	7.03	15	Repayment on maturity
Landesbank Hessen-Thuringen	LOBO	04/02/2000	04/02/2015	11.60	5.68	15	Repayment on maturity
Public Works Loan Board	EIP	22/01/2014	22/01/2039	0.04	3.97	25	Repayment of annual EIP amount re borrowing to fund third party loan
Public Works Loan Board	EIP	22/01/2014	22/01/2039	0.04	3.97	25	
Public Works Loan Board	EIP	22/01/2014	22/01/2039	0.04	3.97	25	
Public Works Loan Board	EIP	22/01/2014	22/01/2039	0.04	3.97	25	
Public Works Loan Board	EIP	22/01/2014	22/01/2039	0.06	3.97	25	
Homes & Communities Agency	Annuity	01/04/1985	01/10/2033	0.02	9.25	49	Repayment of annual annuity amount

Profile of borrowing:

3.2.13 The following graph shows the maturity profile of the Council's loans, including borrowing to fund loans to third parties.



3.2.14 The graph is dominated by a 50 year loan of £125m taken out in March 2012 as part of the HRA self-financing.

3.2.15 The Council has one remaining LOBO loan of £9m, with an interest rate of 4.85%, maturing in February 2066. The loan equates to 4% of the total loan portfolio. It is assigned to the HRA and is represented in the graph by the blue bar on the right hand side.

3.2.16 The presentation differs from that in the treasury indicator for maturity structure of borrowing at Appendix 2, in that the Council's remaining LOBO loan is included at final maturity rather than the next call date. In the current low interest rate environment the likelihood of the interest rates on this loan being raised and the loan requiring repayment at the break period is extremely low.

3.2.17 All the Council's borrowing is at a fixed interest rate which limits the Council's exposure to interest rate fluctuations.

Loan restructuring

3.2.18 When market conditions are favourable long term loans can be restructured to:

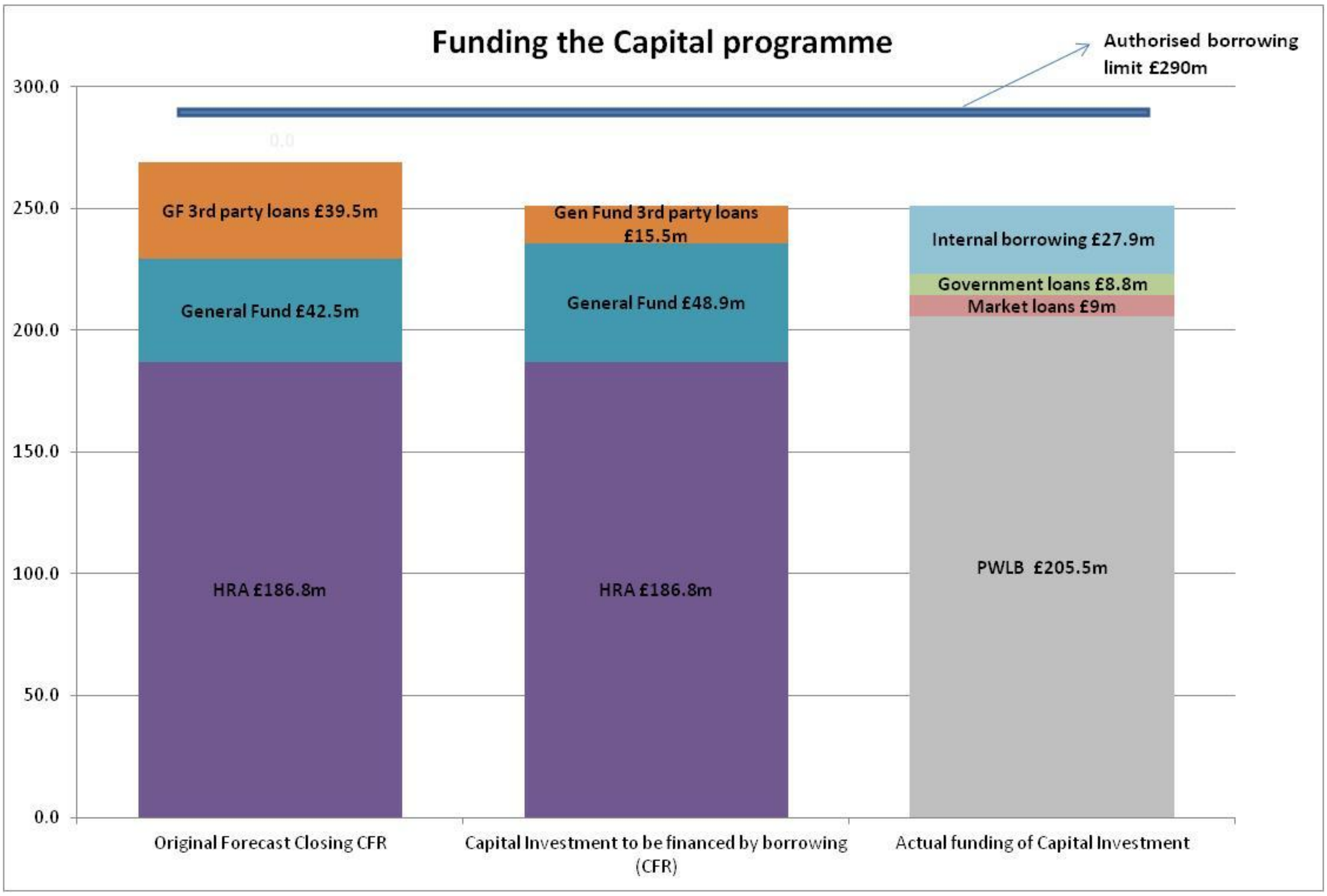
- generate cash savings,
- reduce the average interest rate,
- enhance the balance of the portfolio by amending the maturity profile and/or the level of volatility. (Volatility is determined by the fixed/variable interest rate mix.)

3.2.19 During 2014-15 there were no opportunities for the Council to restructure its borrowing due to the position of the Council's debt portfolio compared to market conditions. Further debt rescheduling will be considered subject to conditions being favourable but it is unlikely that opportunities will present themselves in the near future. The position will be kept under review, and when opportunities for savings do arise, debt rescheduling will be undertaken to meet business needs.

Funding the Capital Programme

3.2.20 The Treasury Management Strategy Statement (TMSS) sets out the plan for treasury management activities over the next year. It identifies where the authority expects to be in terms of borrowing and investment levels. When the 2014-15 TMSS was set, it was anticipated that the Capital Financing Requirement (CFR), the Council's liability for financing the agreed Capital Programme (including loans to third parties), would be £268.8m. This figure is naturally subject to change as a result of changes to the approved capital programme and carry forwards that might occur.

3.2.21 The graph below compares the maximum the Council could borrow in 2014-15 with the forecast CFR at 31 March 2015 and the actual position of how this is being financed as at 31 March 2015.



3.2.22 The graph shows the Council's estimated CFR at budget build and actual CFR at year end split between HRA, General Fund and GF borrowing to fund loans to third parties.

3.2.23 Council's current capital investment financed via borrowing as at 31 March 2015 was £38.8m below the Authorised Borrowing Limit set for by Council at the start of the year.

3.2.24 In addition, the graph shows how the Council is currently financing its borrowing requirement. As at 31 March the Council was using £27.9m of internal borrowing to finance capital investment. Internal borrowing is the use of the Council's surplus cash to finance the borrowing liability instead of borrowing externally. The strategy of internally borrowing, by carefully managing the Councils balance sheet, is currently the most appropriate strategy which enables savings to be generated and reduces the level of cash invested and credit risk associated with investing.

Quarter 1 2015-16

3.2.25 The borrowing position at the end of quarter 1 2015-16 is unchanged from that at 31 March 2015 apart from small movements in temporary borrowing relating to amounts deposited with NBC by two local organisations under long standing arrangements.

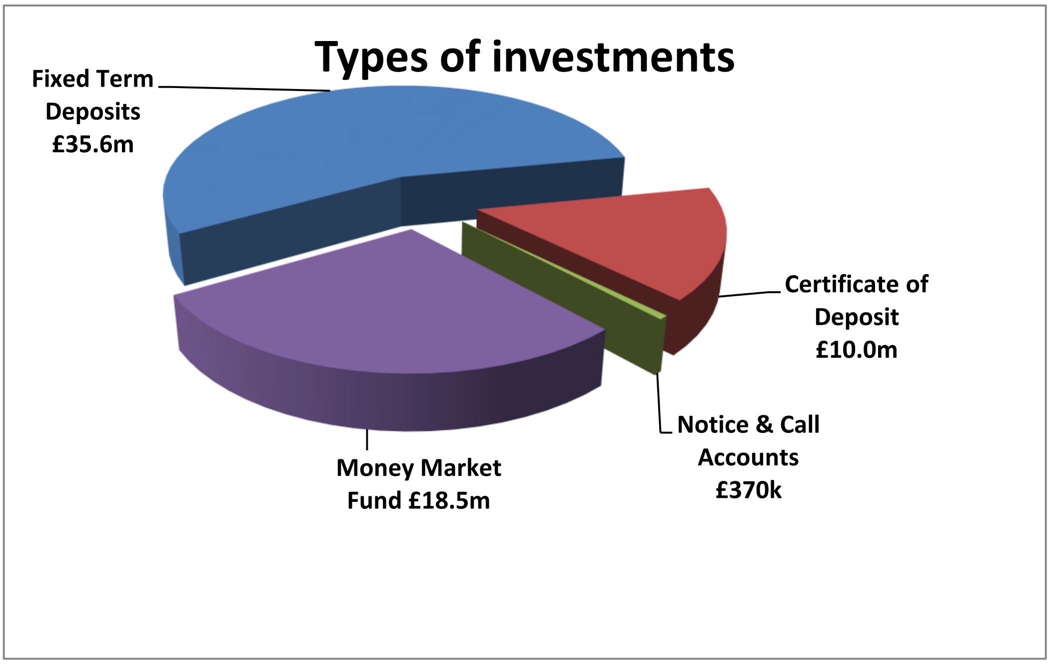
Investments

3.2.26 Investment activity is carried out within the Council's counterparty policies and criteria, and with a clear strategy of risk management in line with the Council's treasury strategy for 2014-15. This ensures that the principle of considering security, liquidity and yield, in that order (SLY), is consistently applied. The Council will therefore aim to achieve the optimum return on investments commensurate with proper levels of security and liquidity. Any variations to agreed policies and practices are reported to Cabinet and Council

3.2.27 The strategy currently employed by the Council of internal borrowing also has the effect of limiting the Council's investment exposure to the financial markets, thereby reducing credit risk.

3.2.28 The Council's investment portfolio as at 31 March 2015 is attached at **Appendix 3**. As at 31 March the level of investment totalled £64.47m. This excludes loans to third parties, which are classed as capital expenditure. The level of cash available for investment is as a result of reserves, balances and working capital the Council holds. These funds can be invested in money market deposits, placed in funds or used to reduce external borrowings.

3.2.29 A breakdown of investments, as at 31 March by type is shown in the graph below. The majority of investments are fixed term deposits with banks for periods up to one year. Investments are made within the boundaries of the Investment Strategy and credit worthiness criteria. The weighted average time to maturity is 148 days.



Investment Performance

3.2.30 The Council's average rate of return on investments in 2014-15 was 0.66%. Performance above the 7 day LIBID (London Interbank Bid Rate) averaged 0.31% against a target of 0.29%. The average differential to 7 day LIBID represents an uplift of £3,100 per £1m invested.

3.2.31 The ability to meet the 7 day LIBID performance target is reliant on the market providing financial products with suitable rates that also comply with the risk requirements set out within the Council's Treasury Management Strategy.

3.2.32 The Council has benchmarked its investment performance against other local authorities, using data from the Capita Investment Benchmarking Forum, which provides quarterly benchmarking data, on a snapshot basis, on investment returns. The following table sets out the Council’s performance compared with other local authorities during 2014-15 using this indicator.

Average Investment Returns 2014-15				
Benchmarking Forum Classification	**30 June 2014**	**30 Sept 2014**	**31 Dec 2014**	**31 March 2015**
Northampton Borough Council	0.67%	0.68%	0.70%	0.73%
Benchmarking Group	0.60%	0.62%	0.64%	0.67%
Non Metropolitan Districts	0.67%	0.69%	0.69%	0.72%
Whole population	0.66%	0.68%	0.68%	0.70%

3.2.33 The NBC performance has been above or in line with the comparator group averages throughout the year. The circumstances and risk appetite of individual local authorities will be reflected in their returns. For example some local authorities will invest in non-rated building societies and consequently have access to higher rates, but with an increased level of risk; others will limit their investments to the least risky counterparties and investment types such as the DMO and/or government gilts, but with a commensurate reduction in returns. The aim is to optimise returns within the parameters of the Council’s Treasury Strategy, which reflects its assessment of risk.

3.2.34 To ensure the Council is maximising the current opportunities contained in the Treasury Management Strategy it will continue to work with its external treasury management advisers to review the position, and if opportunities exist outside of the existing strategy , it will propose these to senior management and members for consideration.

3.2.35 Where appropriate, investments have been locked out for periods of up to one year with nationalised banks (UK Government backed) at higher rates of interest. In a rising interest rate environment it is appropriate to keep investments fairly short in duration so as to take advantage of interest rate rises as soon as they occur.

3.2.36 Leaving market conditions to one side, the Council’s return on investment is influenced by a number of factors, the largest contributors being the duration of investments and the credit quality of the institution or instrument. Credit risk is a measure of the likelihood of default and is controlled through the creditworthiness policy approved by Council. The duration of an investment introduces liquidity risk, the risk that funds can't be accessed when required, and interest rate risk, the risk that arises from fluctuating market interest rates. These factors and associated risks are actively managed by the LGSS Treasury team together with the Council's Treasury Advisors (CAS). Using credit ratings, the investment portfolio's historic risk of default stand at 0.031%. This simply provides a calculation of the possibility of average default against the historical default rates. The Council is also a member of a benchmarking group run by CAS which shows that, for the value of risk undertaken, the returns generated are in line with the Model Band.

Quarter 1 2015-16

3.2.37 Investment balances in quarter 1 of 2015-16 averaged £79m, with a weighted average rate of interest of 0.72%. In terms of performance this was 0.35% (35 basis points) above the average 7 day LIBID, against a target of 0.29% above 7 day LIBID.

Outlook

3.2.38 The Council's treasury advisor, Capita Asset Services, has provided the following forecast of interest rates:

	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18
Bank rate	0.50%	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.50%	1.50%	1.75%
5yr PWLB rate	2.30%	2.40%	2.50%	2.60%	2.80%	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%
10yr PWLB rate	2.90%	3.00%	3.20%	3.30%	3.40%	3.50%	3.70%	3.80%	3.90%	4.00%	4.10%
25yr PWLB rate	3.60%	3.70%	3.80%	4.00%	4.10%	4.20%	4.30%	4.40%	4.40%	4.50%	4.60%
50yr PWLB rate	3.60%	3.70%	3.80%	4.00%	4.10%	4.20%	4.30%	4.40%	4.40%	4.50%	4.60%

3.2.39 Capita Asset Services undertook a review of its interest rate forecasts after the May Bank of England Inflation Report. The ECB's quantitative easing programme to buy up EZ debt caused an initial widespread rise in bond prices and, correspondingly, a fall in bond yields to phenomenally low levels, including the debt of some European countries plunging into negative yields. Since then, fears about recession in the EZ, and around the risks of deflation, have abated and so there has been an unwinding of this initial phase with bond yields rising back to more normal, though still historically low yields.

3.2.40 This latest forecast includes a move in the timing of the first increase in Bank Rate from quarter 1 of 2016 to quarter 2 of 2016 as a result primarily of poor growth in quarter 1, weak wage inflation and the recent sharp fall in inflation due to the fall in the price of oil and the impact of that on core inflation. The UK fell marginally into deflation in April (-0.1%) and figures near zero will prevail for about the next six months until the major fall in oil prices in the latter part of 2014 falls out of the twelve month calculation of CPI inflation. 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 a significant recovery 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.

3.2.41 From a strategic perspective, the Council is continually reviewing options as to the timing of any potential borrowing and also the alternative approaches around further utilising cash balances and undertaking shorter term borrowing which could potentially generate savings subject to an assessment of the interest rate risks involved. Cash flows this year have been sufficiently robust for the Council to use its balance sheet strength and avoid taking on new borrowing.

Third Party Loans

3.2.42 Northampton Town Football Club – Further loan tranches to the value of £5.75m were drawn down by Northampton Town Football Club during the year to support stadia expansion and associated development. Loans under the original facility agreement were granted as maturity loans; drawdowns on the hotel facility loan agreement take the form of annuity loans.

3.2.43 Cosworth - A loan of £1.4m was made to Cosworth to fund the acquisition of machinery at their new factory in the enterprise Zone. Repayments of principal are on an EIP basis.

3.2.44 Unity Leisure – During 2014-15 Cabinet approved the provision of a £300k loan to Northampton Leisure Trust (NLT) to facilitate purchase a soft play facility, based in Northampton. This will be drawn down during 2015-16 and will be cost-neutral to the Council.

3.2.45 University of Northampton –The Council has worked with the South East Midlands Local Enterprise Partnership (SEMLEP) to secure the LEP project rate from PWLB for a loan facility of £46 million to support the creation of a waterside campus. .The loan is now expected to be drawn down during the last quarter of 2015-16. Alongside this Northamptonshire Enterprise Partnership (NEP) has worked with Northamptonshire County Council to secure a further £14m at the LEP project rate from PWLB for the same project.

Debt Financing Budget

3.2.46 The table below shows the budget, outturn and variance for the Council's General Fund debt and investment portfolio in 2014-15. This demonstrates the revenue (current) effects of the treasury transactions executed.

	Budget	Outturn	Variance
	£000	**£000**	**£000**
Interest payable	1,910	1,770	(140)
Interest receivable	(872)	(1,323)	(451)
Soft Loan Accounting Adjustments	(419)	(419)	0
MRP	1,342	1,253	(89)
Recharges from/(to) HRA – interest on balances	136	339	203
Total	**2,097**	**1,620**	**(477)**

3.2.47 The main reasons for the variances were as follows:

- Interest payable – budgeted new and replacement borrowing was actually funded internally from cash balances creating a saving.
- Interest receivable – cash balances and interest rates were both higher than budgeted; interest earned on a third party loan was not anticipated at the start of the year and so not budgeted
- MRP – there was a lower level of funding by borrowing in 2013-14 due to carry forwards in capital programme
- HRA recharges - cash balances and interest rates achieved were both higher than budgeted.

PWLB Governance Arrangements

3.2.48 The Government has tabled an amendment to the infrastructure Bill which would enable the Government to abolish the Public Works Loan Board and transfer its lending to another body using the processes set out in the Public Bodies Act 2011.

3.2.49 The Government plans to set out its proposals on transferring the lending function to another body in a consultation document in due course.

3.2.50 As a Council we have been reassured by the Department for Communities and Local Government that the reform is about the governance only and that that proposals will have no impact on existing loans held by local authorities or the government’s policy on Local Authority borrowing.

Compliance with Treasury Limits and Prudential Indicators

3.2.51 With effect from 1st April 2004 The Prudential Code became statute as part of the Local Government Act 2003 and was revised in 2011.

3.2.52 The key objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of the Council are affordable, prudent and sustainable. To ensure compliance with this the Council is required to set and monitor a number of Prudential Indicators.

3.2.53 During the financial year 2014-15 the Council operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Management Strategy Statement (TMSS) and in compliance with the Council's Treasury Management Practices. The Prudential and Treasury Indicators are shown in **Appendix 2**.

4. Implications (including financial implications)

4.1 Policy

4.1.1 The Council is required to adopt the latest CIPFA Treasury Management Code of Practice, and to set and agree a number of policy and strategy documents. These policy documents are reported to Cabinet and Council as part of the budget setting process. The Council's Treasury Strategy for 2014-15 was approved by Council on 24 February 2014.

4.1.2 This report complies with the requirement to submit an annual treasury management review report to Council.

4.3.2 The CIPFA Treasury Management Code of Practice requires the Council to nominate the body (such as an audit or scrutiny committee) responsible for ensuring effective scrutiny of the treasury management strategy, policies and practices. The Audit Committee has been nominated for this role, which includes the review of all treasury management policies and procedures, the review of all treasury management reports to Cabinet and Council, and for making recommendations to Council.

4.2 Resources and Risk

4.2.1 The resources required for the Council's debt management and debt financing budgets are agreed annually through the Council's budget setting process. The debt financing budget outturn position is shown at paragraph 3.2.46 to 3.2.47.

4.2.2 The risk management of the treasury function is specifically covered in the Council's Treasury Management Practices (TMPs), which are reviewed annually. Treasury risk management forms an integral part of day-to-day treasury activities.

4.2.3 The risk implications of decisions taken and transactions executed during 2014-15 financial year are discussed in the body of the report at paragraph 3.2.4.

4.3 Legal

4.3.1 The Council is obliged to carry out its treasury management activities in line with statutory requirements and associated regulations and professional guidance.

4.4 Equality

4.4.1 An Equalities Impact Assessment was carried out on the Council's Treasury Strategy for 2014-15, and the associated Treasury Management Practices (TMPs) and the Schedules to the TMPs. The EIA assessment is that a full impact assessment is not necessary, as no direct or indirect relevance to equality and diversity duties has been identified

4.5 Consultees (Internal and External)

4.5.1 Consultation on treasury management matters is undertaken as appropriate with the Council's treasury advisors, Sector, and with the Portfolio holder for Finance.

4.5.2 Under the regulatory requirements, the Audit Committee has been nominated by Council as the body responsible for ensuring effective scrutiny of the treasury management strategy, policies and practices. This role includes the review of all treasury management policies and procedures, the review of all treasury management reports to Cabinet and Council, and the making of recommendations to Council. This report will be presented to Audit Committee at their meeting of 9 November 2015.

4.6 How the Proposals deliver Priority Outcomes

4.6.1 The Council has adopted the CIPFA Code of Practice on Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes ("the Treasury Management Code of Practice").

4.6.2 Under the umbrella of the Treasury Management Code of Practice, the Council's Treasury Management Policy Statement "…acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management."

4.6.3 This supports the Council's priority of making every £ go further.

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4.7 Other Implications

4.7.1 No other implications have been identified.

5. Background Papers

None

Glenn Hammons, Chief Finance Officer 0300 330 7000

Appendix 1

Economic Update (provided by CAS Treasury Solutions)

Quarter Ended 30th June 2015

1. The latest economic data showed that the recovery slowed in the first quarter. However, the latest National Accounts painted the recovery in a better light than previously thought. Indeed, Q1's quarterly GDP growth estimate was nudged up from 0.3% to 0.4% on the back of some stronger construction data. What's more, given the strength of the business surveys, we wouldn't be surprised if Q1's growth figure was revised even higher in time.
2. In any case, the surveys suggest that the recovery got swiftly back on track in Q2. On the basis of past form, the average level of the Markit/CIPS composite PMI is consistent with quarterly GDP growth of around 0.8%. And the Bank of England's Agents' scores point to a similarly-strong pick-up. Granted, only limited official data has been published so far for Q2, but April's industrial production and trade figures paint an encouraging picture for the economic recovery at the start of the quarter.
3. Early indicators suggest that the recovery in household spending has maintained plenty of momentum in Q2. Although retail sales volumes rose by just 0.2% on the previous month in May, this followed a 0.9% rise in April. Accordingly, even if sales volumes were unchanged in June, they would still have risen by 0.9% over Q2 as a whole, matching Q1's rise. What's more, spending off the high street looks to have remained robust as well. The Bank of England's Agents' Score of turnover in the services sector points to a further acceleration in nominal spending on services in the near term. In addition, the latest consumer confidence figures suggest that households still think now is a good time to undertake major purchases.
4. Household spending should continue to be supported by developments in the labour market. The ILO unemployment rate has now fallen to 5.5%, not far above pre-crisis levels. And the employment rate is the highest since records began. The significant tightening in the labour market over the past eighteen months or so has begun to feed through into pay, with annual growth in headline average weekly earnings (excluding bonuses) picking up to 2.7% in April, its strongest since February 2009. We expect nominal wage growth to strengthen a bit further over the coming months as the unemployment rate continues to nudge down. The subdued outlook for inflation should underpin real wage growth.

5. The latest consumer prices figures showed that deflation lasted just one month. CPI inflation rose from -0.1% in April to +0.1% in May, reflecting the slower pace of falls in food prices and a rebound in petrol prices. We had stressed for a long while that deflation was likely to be fleeting, as it primarily reflected temporary external factors such as the fall in energy prices and food prices, as well as an appreciation in sterling, rather than weakness in domestic demand. Meanwhile, there have not been any signs that very low inflation has had any adverse second round effects on inflation expectations or spending decisions. Nonetheless, inflation looks set to hover just above zero for the next six months, and it wouldn't take much during that period, perhaps a renewed 10% fall in the oil price, for the UK to be tipped back into deflation.

6. Unsurprisingly, then, the Monetary Policy Committee do not appear to be in any rush to raise interest rates. Granted, the minutes of June's MPC meeting showed that for two members, the decision to leave rates on hold was "finely balanced". And a recent interview with the Financial Times, resident MPC hawk Martin Weale suggested that he is not too far off restoring his vote to raise rates again. But with inflation close to zero, the first budget of the next parliament due to be published in July, and the situation in Greece becoming increasingly troubling, it looks that they will wait at least another few months before turning against the grain again. And with the rest of the committee likely to stand pat for even longer, it looks unlikely that there will be an increase in interest rates this year. Indeed, we still think that the first hike in Bank Rate will occur in Q2 next year, broadly in line with market expectations.

7. Meanwhile, with the Conservatives winning an outright majority in May's general election, the fiscal squeeze is set to re-intensify next year. We will know more detail about the Chancellor's plans at the Budget on the 8th July, but we already know that in order to meet their manifesto pledge, the Conservatives will have to implement a fiscal consolidation worth around 5% of GDP over the next four years. And given that they have pledged to not increase VAT, income tax or national insurance in the next parliament, more of the planned squeeze will have to come through cuts to spending than in the last parliament. Admittedly, these plans may be watered down, but it is clear that fiscal policy will be a hindrance, not a help, to the economic recovery over the next few years, and underlines that monetary policy will have to remain extremely accommodative. Meanwhile, the general election brought with it another cloud to the economic recovery – namely a referendum on the UK's membership of the European Union which could happen during 2016, though a May date now appears unlikely.

8. Internationally, the major development over the past quarter has been the deterioration of the situation in Greece. At the time of writing, the country is still a member of the euro-zone, but its future as part of the single currency

has become increasingly uncertain. Greece urgently needs financial assistance in order to meet its debt repayments, but is unwilling to accept the reforms which creditors demand in exchange for funds. The situation is so severe that emergency capital controls have been imposed in order to stop the Greek banking system from collapsing. It is still possible that Greece and its creditors are able to strike a last-minute deal, but it is clear that this is likely to only offer a short-term solution, and Greece will need to undertake substantial debt restructuring or outright default if it is to return its public finances to a sustainable position in the long run. Whilst the UK's direct economic and financial exposures to Greece are small, there could be an adverse impact on the UK's economy from a wider fallout and period of general financial market instability that would be likely to prevail if a "Grexit" were to occur.

9. Finally, UK equity prices have significantly underperformed their US counterparts since the beginning of Q2, with the FTSE 100 falling by 2.3%, whilst the S&P 500 has fallen by only 0.5%. That said, UK equity prices have performed better than those in Europe, which have been hit by renewed fears of a Grexit. Meanwhile, sterling has remained strong against the euro, due to these fears as well as the ECB's ongoing programme of Quantitative Easing. UK 10-year government bond yields have also increased by about 50 basis points since the beginning of Q2. This probably reflects a confluence of factors, such as easing fears of a prolonged bout of deflation, and growing concerns about the impact of a deterioration in the situation in the euro-zone. In any case, gilt yields had looked too low early this year given the fundamental strength of the economic recovery.

Appendix 2

Prudential & Treasury Indicators – 2014-15 Outturn Position

Background and Definitions

For the background, definitions and risk analysis for the prudential and treasury indicators for 2014-15, please see the Treasury Management Strategy 2014-15 report to Council 24 February 2014.

Prudential Indicators

Affordability

a) **Estimate of the ratio of financing costs to net revenue stream**

Ratio of financing costs to net revenue stream		
	2014-15	2014-15
	Estimate %	Actual 31 March 2015 %
General Fund	8.58%	5.85%
HRA	34.18%	33.81%

The driver for actual financing costs on the General Fund being lower than estimated is an underspend of £477k on the debt financing budget, the reasons for which are set out in the main body of the report.

Actual financing costs on the HRA were broadly in line with budget.

b) **Estimate of the incremental impact of capital investment decisions on the council tax**

Estimates of incremental impact of new capital investment decisions on the Council Tax	
	2014-15
	Estimate £.p
General Fund	2.22

This indicator is set before the start of the financial year, in the context of the budget setting process, which feeds into the setting of Council Tax and Housing Rents. As these are set and fixed for the financial year ahead, any capital investment decisions made during the year cannot impact on the existing Council Tax and Housing rent levels. This means that new capital investment plans approved during the year must be funded externally or from within existing resources.

c) **Estimate of the incremental impact of capital investment decisions on the housing rents**

Estimates of incremental impact of new capital investment decisions on weekly housing rents	
	2014-15
	Estimate £.p
HRA	6.27

This indicator is set before the start of the financial year, in the context of the budget setting process, which feeds into the setting of Council Tax and Housing Rents. As these are set and fixed for the financial year ahead, any capital investment decisions made during the year cannot impact on the existing Council Tax and Housing rent levels. This means that new capital investment plans approved during the year must be funded externally or from within existing resources.

Prudence

d) Net borrowing and the capital financing requirement (CFR)

Gross external debt less than CFR					
	Excluding third party loans			**Including third party loans**	
	2014-15 Budgeted	2014-15 Actual 31 March 2015		2014-15 Budgeted	2014-15 Actual 31 March 2015
	£000	£000		£000	£000
Gross external debt at 30 Nov 2014	216,441	208,568		228,441	224,083
2013-14 Closing CFR	222,454	222,042		234,454	232,042
Changes to CFR:					
2014-15	6,879	13,672		34,380	19,187
2015-16	2,418	10,421		26,418	59,720
2016-17	429	11,205		429	8,759
Adjusted CFR	235,989	257,340		299,490	319,708
Gross external debt less than adjusted CFR	Yes	Yes		Yes	Yes

This is the key indicator of prudence. It is intended to show that external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital requirement for the current and new two financial years.

The forward looking changes to CFR (2015-16 and 2016-17) are estimates that will be firmed up on an ongoing basis as new capital programme expenditure decisions are made and more accurate forecasts on existing schemes in the programme become available.

Gross external debt during the year, and at 31 March 2015, remained below the adjusted Capital Financing Requirement

Capital Expenditure

e) Estimate of capital expenditure

Capital Expenditure		
	2014-15	2014-15
	Estimate £000	Outturn £000
General Fund	18,352	24,504
HRA	46,700	29,965
Total	**65,052**	**54,469**
Loan to Third Parties	27,500	7,150
Total	**92,552**	**61,619**

In the General Fund, the original capital programme expenditure estimate was increased by scheme carry forwards from 2013-14, and the addition of new schemes during the year.

In the HRA, expenditure was below budget and schemes will be carried forward into the 2015-16 capital programme.

Expenditure on loans to third parties was significantly lower than budgeted due to the re-profiling of loans to the University of Northampton scheme into 2015-16.

Full details of the 2014-15 capital outturn, variances and budget carry forwards to 2015-16 are set out in the Finance and Monitoring Outturn Report to Cabinet on 15 July 2015.

f) Estimates of capital financing requirement (CFR)

Capital Financing Requirement (Closing CFR)		
	2014-15	2014-15
	Estimate £000	31 March 2015 Actual £000
General Fund	42,531	48,911
HRA	186,803	186,803
Total	**229,334**	**235,714**
Loan to Third Parties	39,500	15,515
Total	**268,834**	**251,229**

The CFR can be understood as the Council's underlying need to borrow money long term for a capital purpose – that is, after allowing for capital funding from capital receipts, grants, third party contributions and revenue contributions. Changes to the CFR are linked directly to the use of borrowing to finance new capital expenditure (including finance leases), and to the repayment of debt through Minimum Revenue Provision (MRP).

The General Fund CFR at 31 March 2014 is above the estimate due to an increase capital expenditure funded by borrowing for the reasons set out at (e) above.

The HRA CFR has remained unchanged since none of the HRA capital programme in 2014-15 was financed by borrowing.

External Debt

g) Authorised limit for external debt

Authorised Limit for external debt		
	2014-15	2014-15
	Boundary £000	31 March 2015 Actual £000
Borrowing - NBC	245,000	208,072
Borrowing - Third Party Loans	40,000	15,515
Other long-term liabilities	5,000	496
TOTAL	**290,000**	**224,083**

The long term liabilities figure relates to finance leases.

External debt remained below the authorised limit throughout 2014-15.

h) Operational boundary for external debt

Operational boundary for external debt		
	2014-15	2014-15
	Boundary £000	31 March 2015 Actual £000
Borrowing - NBC	235,000	208,072
Borrowing - Third Party Loans	40,000	15,515
Other long-term liabilities	5,000	496
TOTAL	**280,000**	**224,083**

The long term liabilities figure relates to finance leases.

External debt remained below the operational boundary throughout 2014-15.

i) HRA Limit on Indebtedness

HRA Limit on Indebtedness	
2014-15	2014-15
Limit £000	Closing HRA CFR 31 March 2015 £000
208,401	186,803

The HRA limit on indebtedness is £208.401m. This is the HRA debt cap imposed by the Department for Communities and Local Government at the implementation of HRA self-financing. The HRA CFR of £186.803m, which is the measure of indebtedness, is below the limit.

Compliance

j) Adoption of the CIPFA code of Practice for Treasury Management in the Public Services

The Council has adopted CIPFA's Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes. The adoption is included in the Council's Constitution, approved by the Council on 14 March 2011, at paragraph 6.10 of the Financial Regulations

Treasury Indicators

l) Upper limits on interest rate exposures

Upper limits on interest rate exposures - Investments and Borrowing		
	2014-15	2014-15
	Limit %	Actual 31 March 2015 %
Fixed Interest Rate Exposures	150%	106%
Variable Interest Rate Exposures	150%	-6%

Upper limits on interest rate exposures - Investments		
	2014-15	2014-15
	Limit %	Actual 31 March 2015 %
Fixed Interest Rate Exposures	100%	71%
Variable Interest Rate Exposures	100%	29%

Upper limits on interest rate exposures - Borrowing		
	2014-15	2014-15
	Limit %	Actual 31 March 2015 %
Fixed Interest Rate Exposures	100%	96%
Variable Interest Rate Exposures	100%	4%

The purpose of these three indicators is to express the Council's appetite for exposure to variable interest rates, which may, subject to other factors, lead to greater volatility in payments and receipts. However this may be offset by other benefits such as lower rates. Separate indicators have been set and monitored for debt and investments, as well as for the net borrowing position. Maximum exposure for fixed and variable rates during the year may add up to more than 100% (or 150% in the case of the combined indicator) as each is likely to occur on a different date. Actual exposure at 31 March 2015, and during the year, remained within the agreed limits.

m) Total principal sums invested for periods longer than 364 days

Upper limit on investments for periods longer than 364 days		
	2014-15	2014-15
	Upper Limit £000	Actual 31 March 2015 £000
Investments longer than 364 days	6,000	2,500

Investment periods have generally been kept to 364 days or below to maintain liquidity and to minimise counterparty risk in line with the Council's treasury strategy.

k) Maturity Structure of Borrowing

Maturity structure of borrowing			2014-15	2015-15
	Lower Limit %	Upper Limit %	Actual 31 March 2015 %	Actual 31 March 2015 £000
Under 12 months	0%	20%	1%	2,339
1-2 years	0%	20%	3%	6,296
2-5 years	0%	20%	8%	16,932
5-10 years	0%	20%	13%	28,522
10-20 years	0%	40%	15%	34,224
20-30 years	0%	60%	1%	1,200
30-40 years	0%	80%	0%	-
Over 40 years	0%	100%	60%	134,116

The Treasury Management Code of Practice requires the maturity of borrowing to be determined by reference to the earliest date on which the lender can require payment.

The Council's one remaining LOBO loan is presented as maturing within 12 months, due to the six monthly break clauses, whereby the lender can opt to increase the rate, and the Council can choose to accept or decline the new rate. However in the current interest rate environment it is not to the lender's advantage to increase the rate at the break dates and this option is not likely to be exercised.

Appendix 3

NBC Investment Portfolio as at 31 March 2015

Type	Start Date	Maturity Date	Counterparty	Profile	Rate	Principal O/S (£)
Fixed	22/04/14	21/04/15	Bank of Scotland plc	Maturity	0.9500%	-2,000,000.00
Fixed	21/05/14	20/05/15	Bank of Scotland plc	Maturity	0.9500%	-3,000,000.00
Fixed	27/08/14	26/08/15	Bank of Scotland plc	Maturity	0.9500%	-3,000,000.00
Fixed	09/09/14	09/06/15	DBS Bank Ltd	Maturity	0.6500%	-4,000,000.00
Fixed	09/09/14	08/09/15	Bank of Scotland plc	Maturity	0.9500%	-2,000,000.00
Fixed	30/09/14	30/09/15	East Lothian Council	Maturity	0.7000%	-3,000,000.00
Fixed	14/11/14	14/05/15	Credit Suisse AG	Maturity	0.6500%	-5,000,000.00
Fixed	16/12/14	16/12/16	Blaenau Gwent County Borough Council	Maturity	0.9300%	-2,500,000.00
Fixed	12/12/14	04/06/15	Royal Bank of Scotland plc	Maturity	0.9400%	-5,000,000.00
Fixed	07/01/15	06/01/16	Bank of Scotland plc	Maturity	1.0000%	-2,500,000.00
Fixed	16/02/15	15/02/16	Bank of Scotland plc	Maturity	1.0000%	-2,500,000.00
Fixed	20/02/15	19/02/16	DBS Bank Ltd	Maturity	0.7000%	-3,000,000.00
Fixed	26/02/15	25/02/16	Bank of Scotland plc	Maturity	1.0000%	-3,000,000.00
Fixed	26/03/15	24/03/16	Bank of Scotland plc	Maturity	1.0000%	-2,000,000.00
Fixed	12/03/15	10/09/15	Nationwide Building Society	Maturity	0.6600%	-3,000,000.00
Fixed Total						**-45,500,000.00**
Call	31/03/14		HSBC Bank plc	Maturity	0.0500%	-370,000.00
Call Total						**-370,000.00**
MMF	31/03/14		Ignis Sterling Liquidity 2 GBP	Maturity	0.4734%	-15,000,000.00
MMF	31/03/14		Insight Liquidity Sterling C3	Maturity	0.4352%	-1,335,000.00
MMF	01/07/14		LGIM Sterling Liquidity 4	Maturity	0.4348%	-2,138,000.00
MMF Total						**-18,473,000.00**
						-64,343,000.00