DEVON & SOMERSET
FIRE & RESCUE AUTHORITY

REPORT REFERENCE NO.	**DSFRA/14/11**
MEETING	**DEVON & SOMERSET FIRE & RESCUE AUTHORITY (Ordinary Meeting)**
DATE OF MEETING	**29 MAY 2014**
SUBJECT OF REPORT	**ANNUAL TREASURY MANAGEMENT REPORT 2013-14**
LEAD OFFICER	**Treasurer**
RECOMMENDATIONS	***That the performance in relation to the treasury management activities of the Authority for 2013-2014, as set out in this report, be noted.***
EXECUTIVE SUMMARY	The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management, requires that the Authority receives a report in respect of borrowing and investment activities during the year, and compares this performance against the treasury management strategy adopted. The report includes a performance report relating to the 2013-14 financial year.
RESOURCE IMPLICATIONS	As indicated in the report.
EQUALITY RISKS AND BENEFITS ANALYSIS (ERBA)	The contents of this report are considered compatible with equalities and human rights legislation.
APPENDICES	A. Prudential indicators 2013-14.
LIST OF BACKGROUND PAPERS	Treasury Management Strategy (including Prudential and Treasury Indicators) Report DSFRA/13/3

1. INTRODUCTION

1.1 The Authority is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2013-14. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

1.2 The Authority fully complies with the primary requirements of the Code, which includes:

- The creation and maintenance of a Treasury Management Policy Statement, which sets out the policies and objectives of the Authority's treasury management activities.
- The creation and maintenance of Treasury Management Practices, which set out the manner in which the Authority will seek to achieve those policies and objectives.
- The receipt by the Authority of an annual strategy report for the year ahead, a mid year treasury update report and an annual review report of the previous year.
- The delegation by the Authority of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
- Delegation by the Authority of the role of scrutiny of treasury management strategy and policies to a specific named body which in this Authority is the Resources Committee.

1.3 The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

1.4 The Treasury Management Strategy for Devon & Somerset Fire & Rescue Authority has been underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) 2011 Treasury Management in Public Services Code of Practice (the Code) and the CIPFA Prudential Code.

1.5 Treasury management in this context is defined as:

"The management of the local Authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks. "

2. THE ECONOMY AND INTEREST RATES

2.1 The financial year 2013-14 continued the challenging investment environment of previous years, namely low investment returns, although levels of counterparty risk had subsided somewhat. The original expectation for 2013/14 was that Bank Rate would not rise during the year and for it only to start gently rising from quarter 1 2015. This forecast rise has now been pushed back to a start in quarter 3 2015.

2.2 Economic growth (GDP) in the UK was virtually flat during 2012-13 but surged strongly during the year. Consequently there was no additional quantitative easing during 2013-14 and Bank Rate ended the year unchanged at 0.5% for the fifth successive year. While CPI inflation had remained stubbornly high and substantially above the 2% target during 2012, by January 2014 it had, at last, fallen below the target rate to 1.9% and then fell further to 1.7% in February. It is also expected to remain slightly below the target rate for most of the two years ahead.

2.3 Gilt yields were on a sharply rising trend during 2013 but volatility returned in the first quarter of 2014 as various fears sparked a flight to quality (see paragraph 4.) The Funding for Lending Scheme, announced in July 2012, resulted in a flood of cheap credit being made available to banks which then resulted in money market investment rates falling drastically in the second half of that year and continuing into 2013-14. That part of the Scheme which supported the provision of credit for mortgages was terminated in the first quarter of 2014 as concerns rose over resurging house prices.

2.4 The UK coalition Government maintained its tight fiscal policy stance but recent strong economic growth has led to a cumulative, (in the Autumn Statement and the March Budget), reduction in the forecasts for total borrowing, of £97bn over the next five years, culminating in a £5bn surplus in 2018-19.

2.5 The EU sovereign debt crisis subsided during the year and confidence in the ability of the Eurozone to remain intact increased substantially. Perceptions of counterparty risk improved after the ECB statement in July 2012 that it would do “whatever it takes” to support struggling Eurozone countries; this led to a return of confidence in its banking system which has continued into 2013/14 and led to a move away from only very short term investing. However, this is not to say that the problems of the Eurozone, or its banks, have ended as the zone faces the likelihood of weak growth over the next few years at a time when the total size of government debt for some nations is likely to continue rising. Upcoming stress tests of Eurozone banks could also reveal some areas of concern.

3. <u>OVERALL TREASURY POSITION AS AT 31 MARCH 2014</u>

3.1 The Authority’s debt and investment position at the beginning and the end of the year was as follows:

SUMMARY	31st March 2013 Principal	Rate/ Return	31st March 2014 Principal	Rate/ Return
Total Debt - PWLB	*£27.167m*	*4.227%*	*£26.214m*	*4.231%*
CFR	*£26.307m*		*£24.382m*	
Over/(under) borrowing	*£0.860m*		*£1.832m*	
Total Investments	*£17.792m*	*0.64%*	*£25.107m*	*0.61%*
NET DEBT	*£9.375m*		*£0.725m*	

3.2 As is indicated above actual levels of external borrowing of £26.214m as at 31 March 2014, exceeds the CFR figure of £24.382m, which reflects that borrowing of £1.832m has been taken out in advance of spending. This is as a result of capital slippage against the 2013-14 programme being more than forecast, and it is forecast that capital spending in the next two years will increase the CFR sufficiently to reverse this over borrowing position. At this time this does not represent a breach of prudential indicators, as borrowing is permitted up to what is called the Authorised Limit i.e. £32.770m, and therefore no action is required.

4. <u>STRATEGY FOR 2013-14</u>

4.1 The expectation for interest rates within the strategy for 2013-14 anticipated low but rising Bank Rate (starting in quarter 1 of 2015), and gradual rises in medium and longer term fixed borrowing rates during 2013-14. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

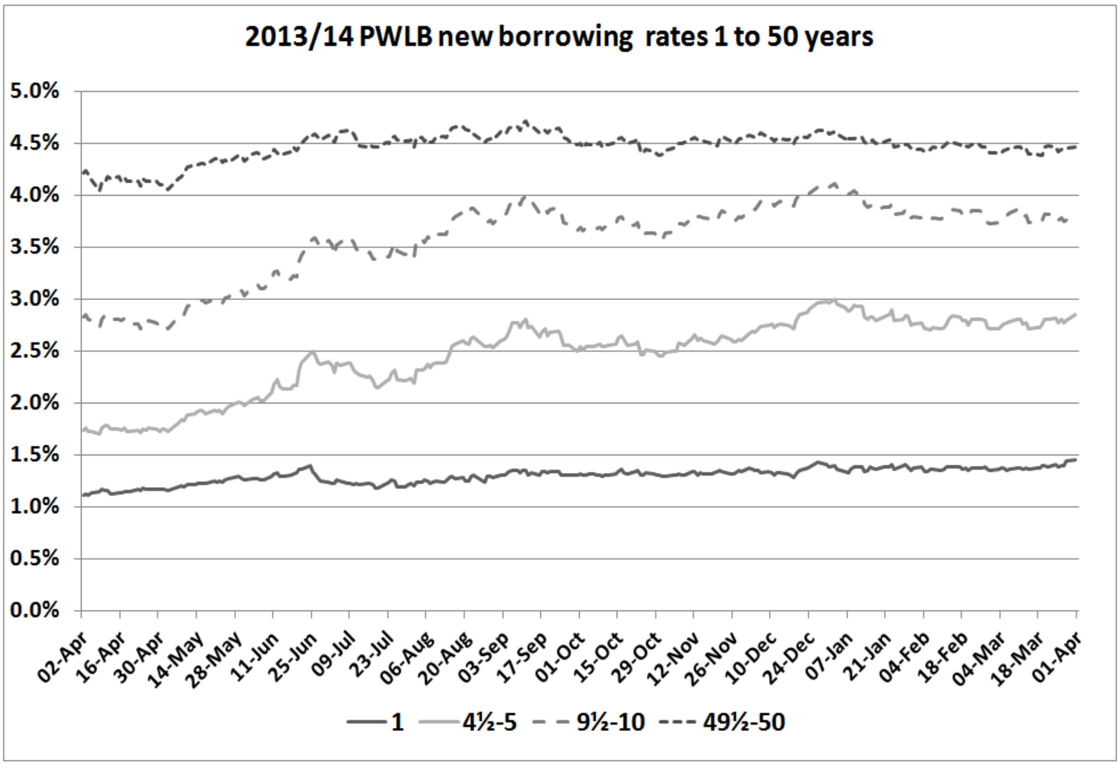
4.2 Based upon these circumstances, the treasury strategy was to postpone borrowing to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

4.3 The actual movement in gilt yields meant that PWLB rates were on a sharply rising trend during 2013 as markets anticipated the start of tapering of asset purchases by the Fed. This duly started in December 2013 and the US FOMC (the Fed.), adopted a future course of monthly reductions of $10bn (from a starting position of $85bn), meaning that asset purchases were likely to stop by the end of 2014. However, volatility set in during the first quarter of 2014 as fears around emerging markets, various vulnerabilities in the Chinese economy, the increasing danger for the Eurozone to drop into a deflationary spiral, and the situation in the Ukraine, caused rates to dip down, reflecting a flight to quality into UK gilts.

5. <u>BORROWING</u>

Public Works Loan Board (PWLB) borrowing rates 2013-2014

5.1 The graph overleaf shows how PWLB borrowing rates have risen from historically very low levels during the year.



DSFRA Borrowing Strategy

Prudential Indicators

5.2 It is a statutory duty for the Authority to determine and keep under review the "Affordable Borrowing Limits". The Authority's' approved Prudential Indicators (affordability limits) are outlined in the approved Treasury Management Strategy.

5.3 During the financial year DSFRA operated within the treasury limits and Prudential Indicators set out in the Authority's annual Treasury Strategy Statement. The outturn for the Prudential Indicators is shown in Appendix A.

DSFRA Borrowing during and at the end of 2013-2014

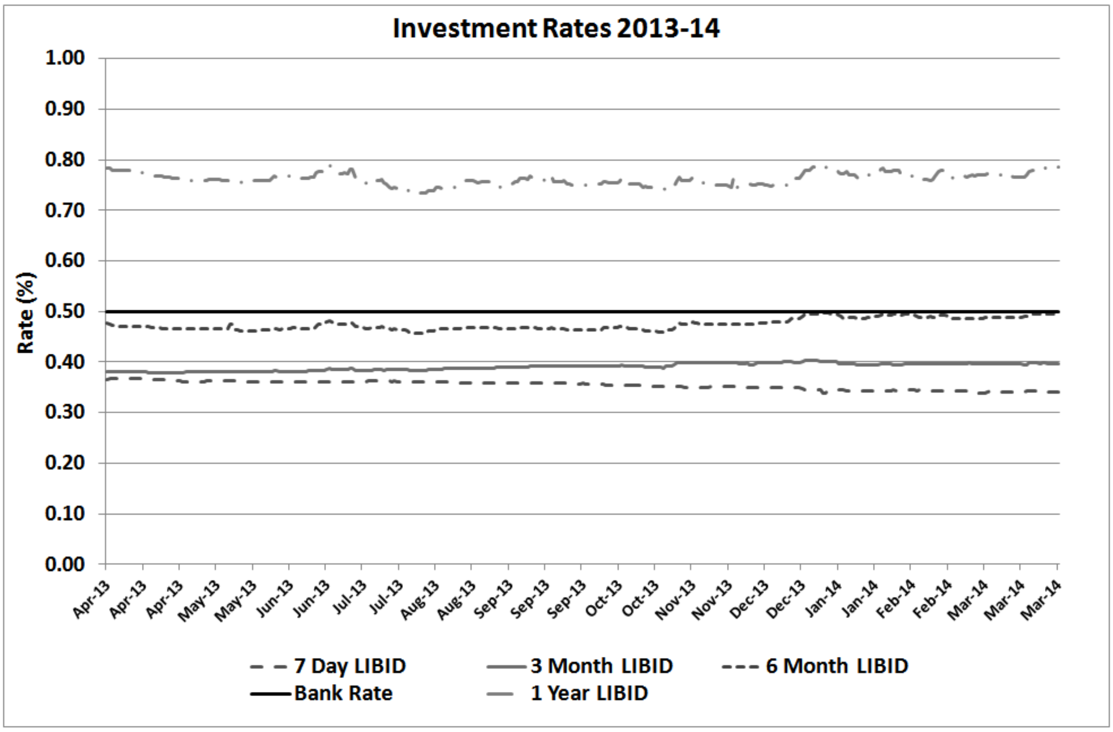
5.4 No new borrowing was taken out in 2013-14 to support capital spending. A summary of the loan (debt) position of the Authority is given in the table below. All existing borrowing has been taken out at Fixed Interest Rates.

	Summary of loan movements during 2013-14		
		Amount £m	
	Value of loans outstanding as at 1/4/13	**27.167**	
	Loans taken during 2013-2014	0.00	
	Loans repaid upon maturity during 2013-14	(0.953)	
	Loans rescheduled during 2013-14	0	
	Total value of loans outstanding as at 31/3/2014	**26.214**	

6. INVESTMENTS

Investment rates in 2013-14

6.1 Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for five years. Market expectations as to the timing of the start of monetary tightening ended up unchanged at early 2015. The Funding for Lending Scheme resulted in deposit rates remaining depressed during the whole of the year, although the part of the scheme supporting provision of credit for mortgages came to an end in the first quarter of 2014.



DSFRA Investment Strategy

6.2 The Authority's Annual Investment Strategy, which is incorporated in the Treasury Management Strategy Statement, outlines the Authority's investment priorities as follows:

- Security of Capital
- Liquidity

6.3 The Authority will also aim to achieve the optimum return on investments commensurate with the proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term, and only invest with highly credit rated financial institutions using the Sector suggested creditworthiness matrices, including Credit Default Swap (CDS) overlay information provided by Sector. In addition to this approach the Authority has the ability to use building societies under specified and non-specified investments.

DSFRA Investments during and at the end of 2013-2014

6.4 No institutions in which investments were made during 2013-2014 had any difficulty in repaying investments and interest in full during the year and the Authority had no liquidity difficulties.

6.5 A full list of investments held as at 31 March 2014 are shown in the table overleaf

Investments as at 31 March 2014					
Counterparty	Maximum to be invested	Total amount invested	Call or Term	Period invested	Interest rate(s)
	£m	£m			
Bank of Scotland	5.000	2.000	T	9 mths	0.83%
		1.500	T	1 yr	0.95%
		1.500	T	9 mths	0.80%
Barclays	10.000	2.000	T	3 mths	0.44%
		1.000	T	3 mths	0.44%
		2.000	T	6 mths	0.54%
National Westminster Bank	5.000	5.000	T	3 mths	0.60%
Svenska Handelsbanken	5.000	5.000	C	Instant Access	Variable
Black Rock Money Market Funds	5.000	0.846	C	Instant Access	Variable
Federated Prime Rate Money Market Funds	5.000	4.261	C	Instant Access	Variable
Total invested as at 31st March 2014		**25.107m**			

6.6 Funds available for investment are on a temporary basis, the level of which are dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme.

Benchmark	**Average level of funds available for Investment**	**Benchmark Return**	**Authority Performance**	Investment Interest Earned
3 month	£28.477m	0.39%	0.43%	£0.173m

6.7 The amount of investment income earned of £0.173m has exceeded the target by £0.073m as a result of levels of fund available for investment during the year being higher than anticipated.

7. SUMMARY

7.1 In compliance with the requirements of the CIPFA Code of Practice of Treasury Management, this report provides members with a summary report of the treasury management activities during 2013-2014. As is indicated in this report, none of the Prudential Indicators have been breached, and a prudent approach has been taken in relation to investment decisions taken during the year, with priority being given to liquidity and security over yield.

7.2 Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments continued to be dominated by risk considerations resulting in relatively low returns compared to borrowing rates. Even so, the Authority is able to report that its returns are above the LIBID 3 month rate, the benchmark return for this type of short term investments.

KEVIN WOODWARD
Treasurer

PRUDENTIAL INDICATOR	2012-13 £m actual	2013-14 £m approved	2013-14 £m actual
Capital Expenditure			
Non - HRA	4.662	6.798	3.853
HRA (applies only to housing authorities)	0	0	0
TOTAL	4.662	6.798	3.853
Ratio of financing costs to net revenue stream			
Non - HRA	3.66%	3.85%	3.75%
HRA (applies only to housing authorities)	0%	0%	0%
Capital Financing Requirement as at 31 March (borrowing only)			
Non – HRA	26.307	25.978	24.382
HRA (applies only to housing authorities)	0	0	0
TOTAL	26.307	25.978	24.382
Annual change in Cap. Financing Requirement			
Non – HRA	0.164	(0.356)	(1.952)
HRA (applies only to housing authorities)	0	0	0
TOTAL	0.164	(0.356)	(1.952)
Incremental impact of capital investment decisions	**£ p**	**£ p**	**£ p**
Increase/(decrease) in council tax (band D) per annum	(£0.55)	(£0.36)	£(0.34)
TREASURY MANAGEMENT PRUDENTIAL INDICATORS			
	£m	**£m**	**£m**
Authorised Limit for external debt -			
borrowing	29.211	32.770	32.770
other long term liabilities	1.587	1.520	1.520
TOTAL	30.798	34.290	34.290
Operational Boundary for external debt -			
borrowing	27.791	32.739	32.739
other long term liabilities	1.509	1.509	1.509
TOTAL	29.300	34.248	34.248

	Actual 31st March 2014	upper limit %	lower limit %
Limits on borrowing at fixed interest rates	100%	100%	70%
Limits on borrowing at variable interest rates	0%	30%	0%
Maturity structure of fixed rate borrowing during 2013-14			
Under 12 months	3.51%	30%	0%
12 months and within 24 months	0.99%	30%	0%
24 months and within 5 years	1.15%	50%	0%
5 years and within 10 years	5.03%	75%	0%
10 years and above	89.31%	100%	50%