

REPORT REFERENCE NO.	DSFRA/16/14
MEETING	DEVON & SOMERSET FIRE & RESCUE AUTHORITY (ORDINARY MEETING)
DATE OF MEETING	26 MAY 2016
SUBJECT OF REPORT	ANNUAL TREASURY MANAGEMENT REPORT 2015-16
LEAD OFFICER	Treasurer
RECOMMENDATIONS	<i>That the performance in relation to the treasury management activities of the Authority for 2015-16, as set out in this report, be noted.</i>
EXECUTIVE SUMMARY	<p>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.</p> <p>The report includes a performance report relating to the 2015-16 financial year.</p>
RESOURCE IMPLICATIONS	As indicated within the report.
EQUALITY RISK AND BENEFIT ASSESSMENT (ERBA)	An initial assessment has not identified any equality issues emanating from this report.
APPENDICES	A. Prudential indicators 2015-16.
LIST OF BACKGROUND PAPERS	Treasury Management Strategy (including Prudential and Treasury Indicators) Report to budget meeting held on the 20 th February 2015 DSFRA/15/3

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 2015-16. 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 During 2015-16 the minimum reporting requirements were that the full Authority should receive the following reports:
- an annual treasury strategy in advance of the year (Authority meeting 20/02/2015).
 - a mid-year (minimum) treasury update report (Authority meeting 14/12/2015).
 - an annual review following the end of the year describing the activity compared to the strategy (this report).
- 1.4 In addition, the Resources Committee has received quarterly treasury management update reports on 02/09/2015, 19/11/2015 and 10/02/2016.
- 1.5 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 Authority's policies previously approved by members.
- 1.6 The Treasury Management Strategy for the 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.
- 1.7 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 Market expectations for the first increase in Bank Rate moved considerably during 2015-16, starting at quarter 3 2015 but soon moving back to quarter 1 2016. However, by the end of the year, market expectations had moved back radically to quarter 2 2018 due to many fears including concerns that China's economic growth could be heading towards a hard landing; the potential destabilisation of some emerging market countries particularly exposed to the Chinese economic slowdown; and the continuation of the collapse in oil prices during 2015 together with continuing Eurozone growth uncertainties.
- 2.2 These concerns have caused sharp market volatility in equity prices during the year with corresponding impacts on bond prices and bond yields due to safe haven flows. Bank Rate, therefore, remained unchanged at 0.5% for the seventh successive year. Economic growth (GDP) in 2015-16 has been disappointing with growth falling steadily from an annual rate of 2.9% in quarter 1 2015 to 2.1% in quarter 4.
- 2.3 The sharp volatility in equity markets during the year was reflected in sharp volatility in bond yields. However, the overall dominant trend in bond yields since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have repeatedly been revised downwards and expectations of increases in central rates have been pushed back. In addition, a notable trend in the year was that several central banks introduced negative interest rates as a measure to stimulate the creation of credit and hence economic growth.
- 2.4 The European central Bank (ECB) commenced a full blown quantitative easing (QE) programme of purchases of Eurozone government and other bonds starting in March at €60bn per month. This put downward pressure on Eurozone bond yields. There was a further increase in this programme of QE in December 2015.
- 2.5 As for America, the economy has continued to grow healthily on the back of resilient consumer demand. The first increase in the central rate occurred in December 2015 since when there has been a return to caution as to the speed of further increases due to concerns around the risks to world growth.
- 2.6 The UK elected a majority Conservative Government in May 2015, removing one potential concern but introducing another due to the promise of a referendum on the UK remaining part of the EU. The government maintained its tight fiscal policy stance but the more recent downturn in expectations for economic growth has made it more difficult to return the public sector net borrowing to a balanced annual position within the period of this parliament.

3. OVERALL TREASURY POSITION AS AT 31 MARCH 2016

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

SUMMARY	31st March 2015 Principal	Rate/ Return	31st March 2016 Principal	Rate/ Return
Total Debt - PWLB	£25.944m	4.231%	£25.817m	4.231%
CFR	£22.582m		£25.818m	
Over/(under) borrowing	£3.362m		(£0.001)m	
Total Investments	£30.956m	0.49%	£27.325m	0.56%
NET DEBT	£(5.012)m		£(1.508)m	

4. **STRATEGY FOR 2015-16**

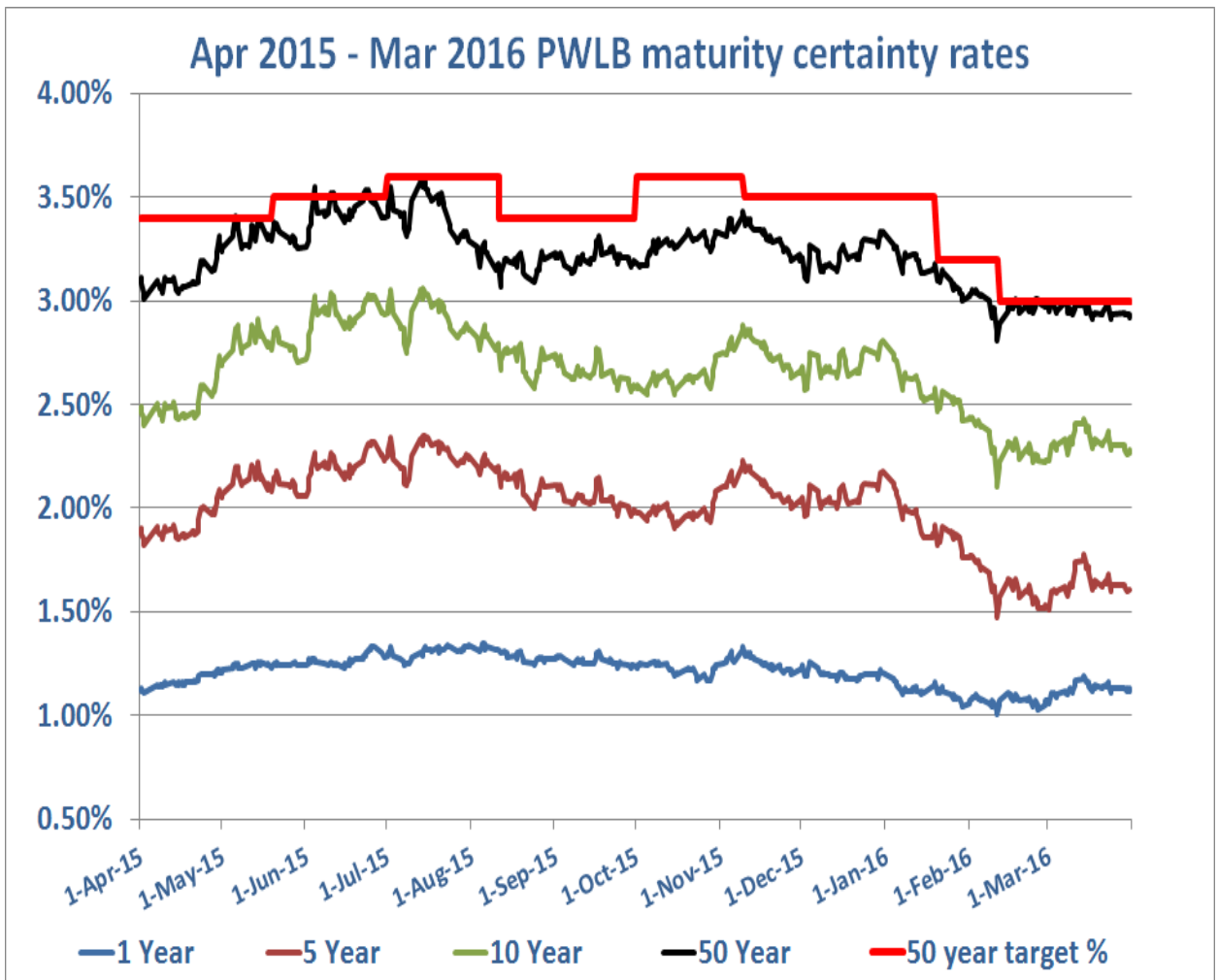
4.1 The expectation for interest rates within the strategy for 2015-16 anticipated low but rising Bank Rate (starting in quarter 1 of 2016), and gradual rises in medium and longer term fixed borrowing rates during 2015-16. Variable, or short-term rates, were expected to be the cheaper form of borrowing 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 In this scenario the strategy was to postpone new borrowing and bring the level of external loans in line with the Capital Financing Requirement as at 31st March 2016. If short term interest rates remain low, the Authority will borrow internally to avoid the cost of holding higher levels of investment and to reduce counterparty risk.

5. **BORROWING**

Public Works Loan Board (PWLB) borrowing rates 2015-16

5.1 The graph below shows how PWLB certainty rates have fallen to 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 the Authority operated within the treasury limits and Prudential Indicators set out in its annual Treasury Strategy Statement. The outturn for the Prudential Indicators is shown in Appendix A.

Authority borrowing during and at the end of 2015-2016

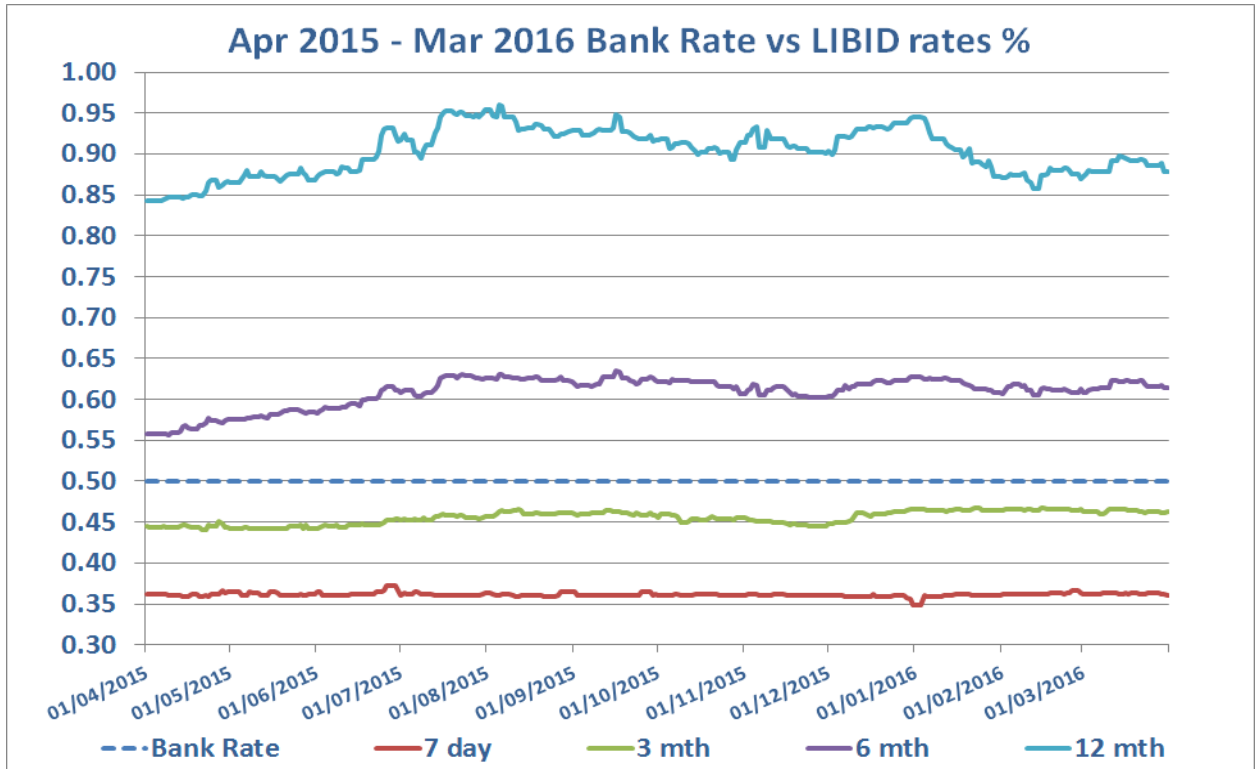
- 5.4 No new borrowing was taken out in 2015-16 to support capital spending and therefore, because repayments of £0.127m loan principal have been made in year, the value of loans outstanding has decreased to £25.817m during the year. A summary of the loan (debt) position of the Authority is given in the table below. All existing borrowing has been taken out at Fixed Interest Rates.
- 5.5 It is noted that the external borrowing figure of £25.817m as 31 March 2016 is within the Capital Financing Requirement (CFR) which means that there is no over-borrowing position at the year-end. This compares to an over-borrowing position of £3.361m at the end of the previous financial year as a result of borrowing taken out in advance of spending. As reported to the Authority at its meeting in May 2015, in considering the final Treasury Management Performance Report for 2015-16, this does not represent a breach of prudential indicators, as borrowing is permitted to be above current Capital Financing Requirement as long as future Capital Financing Requirement estimates for current and next two financial years will utilise these loans.

Summary of loan movements during 2015-16			
		Amount £m	
	Value of loans outstanding as at 1/4/2015	25.944	
	Loans taken during 2015-16	0.00	
	Loans repaid upon maturity during 2015-16	(0.127)	
	Loans rescheduled during 2015-16	0	
	Total value of loans outstanding as at 31/3/2016	25.817	

6. INVESTMENTS

Investment rates in 2015-16

- 6.1 Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for seven years. Market expectations as to the timing of the start of monetary tightening started the year at quarter 1 2016 but then moved back to around quarter 2 2018 by the end of the year. Deposit rates remained depressed during the whole of the year, primarily due to the effects of the Funding for Lending Scheme and due to the continuing weak expectations as to when Bank Rate would start rising.



Authority 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 our Treasury Management Advisors (Capita) suggested creditworthiness matrices, including Credit Default Swap 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.

Authority Investments during and at the end of 2015-16

6.4 No institutions in which investments were made during 2015-16 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 2016 are shown in the table below:

Investments as at 31 March 2016					
Counterparty	Maximum to be invested	Total amount invested	Call or Term	Period invested	Interest rate(s)
	£m	£m			
Bank of Scotland	5.000	2.100	T	1 yr	1.000%
		1.400	T	1 yr	1.000%
		1.500	T	1 yr	1.020%
Barclays	8.000	2.000	T	6 mths	0.690%
		4.000	T	6 mths	0.660%
Santander UK PLC	5.000	1.000	T	6 mths	0.600%
		2.000	T	3 mths	0.690%
		2.000	T	6 mths	0.690%
Coventry Building Society	2.000	2.000	T	6 mths	0.600%
Nationwide Building Society	2.000	2.000	T	6 mths	0.660%
Black Rock Money Market Fund	5.000	3.620	C	Instant Access	Variable
Ignis Sterling Liquidity Money Market Fund	5.000	1.705	C	Instant Access	Variable
Qatar National Bank	2.000	1.000	T	1 yr	1.000%
Local Authority	5.000	1.000	T	3 mths	0.400%
Total invested as at 31 March 2016		£27.325M			

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	£34.400m	0.44%	0.56%	£0.208m

6.7 The amount of investment income earned of £0.208m has exceeded the target by £0.091m 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 2015-15. 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 London Inter-Bank Bid Rate 3 month rate, the benchmark return for this type of short term investments.

KEVIN WOODWARD
Treasurer

APPENDIX A TO REPORT DSFRA/16/14

PRUDENTIAL INDICATOR	2014-15 £m actual	2015-16 £m approved	2015-16 £m Actual
Capital Expenditure			
Non - HRA	2.797	8.202	6.171
HRA (applies only to housing authorities)	0	0	0
TOTAL	2.797	8.202	6.171
Ratio of financing costs to net revenue stream			
Non - HRA	3.62%	3.76%	3.64%
HRA (applies only to housing authorities)	0%	0%	0%
Capital Financing Requirement as at 31 March (borrowing only)			
Non – HRA	22.582	25.818	25.817
HRA (applies only to housing authorities)	0	0	0
TOTAL	22.582	25.818	25.817
Annual change in Cap. Financing Requirement			
Non – HRA	(1.823)	3.169	3.235
HRA (applies only to housing authorities)	0	0	0
TOTAL	(1.823)	3.169	3.235
Incremental impact of capital investment decisions	£ p	£ p	£ p
Increase/(decrease) in council tax (Band D) per annum	(£0.49)	(£0.10)	£(0.10)
TREASURY MANAGEMENT PRUDENTIAL INDICATORS			
	£m	£m	£m
Authorised Limit for external debt - borrowing	31.021	29.477	29.477
other long term liabilities	1.509	1.516	1.516
TOTAL	32.530	30.993	30.993
Operational Boundary for external debt - borrowing	29.948	28.186	28.186
other long term liabilities	1.374	1.444	1.444
TOTAL	31.322	29.630	29.630

	Actual 31 st March 2016	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 2014-15			
Under 12 months	0.49%	30%	0%
12 months and within 24 months	0.36%	30%	0%
24 months and within 5 years	1.08%	50%	0%
5 years and within 10 years	8.22%	75%	0%
10 years and above	89.86%	100%	50%