	London Borough of Hammersmith & Fulham **COUNCIL** **22 OCTOBER 2014**

TREASURY REPORT 2013/14 OUTTURN

Report of the Executive Director of Finance & Corporate Governance

Open Report

Classification - For Information

Key Decision: No

Wards Affected: All

Accountable Executive Director: Jane West Executive Director of Finance & Corporate Governance

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1. EXECUTIVE SUMMARY

1.1. This report presents the Council's outturn Treasury Report for 2013/14 in accordance with the Council's treasury management practices. It is a regulatory requirement for this outturn report to be presented to the Audit, Pensions & Standards Committee by the 30 September each year.

1.2. There are two aspects of Treasury performance – debt management and cash investments. Debt management relates to the Council's borrowing and cash investments to the investment of surplus cash balances. This report covers:

- the treasury position as at 31 March 2014 which includes the investment and the borrowing strategy and outturn for 2013/14;
- the UK economy and interest rates
- compliance with treasury limits and prudential indicators.

1.3. The borrowing amounts outstanding and cash investment for the relevant periods are as follows in the table below.

	2013/14 £m	2012/13 £m	2011/12 £m
Total borrowing	250.51	262.07	262.17
Total cash balances	320.20	206.17	109.30

2. RECOMMENDATION

2.1 That Council is asked to note this report.

3. TREASURY POSITION AS AT 31 MARCH 2014

Investments

3.1. The table below provides a breakdown of the cash deposits, together with comparisons from the previous two years.

Investment Type	2013/14 £m	2012/13 £m	a2011/12 £m
Liquid Deposits	**-**	44.52	18.80
Money Market Funds	39.20	40.00	21.00
Notice Accounts	25.00	-	-
Custodian Held Assets	189.50	-	-
Term Deposits	66.50	121.65	69.50
Total	**320.20**	**206.17**	**109.30**

The total investments increased by over £114 million in 2013/14, the increase was primarily attributable to a rise in usable reserves (£29.748m) and unapplied capital receipts (£81.617m) received in year as shown below in 3.4.

At the end of the year the various investment types were made up of:

- £39.2 million invested in four money market funds run by Goldman Sachs, Blackrock, Insight and Prime Rate. The funds returned an average of 0.38 per cent (all rated AAA by at least two rating agencies) and allow for access on same or next day basis.

- £25 million in Nat West 95 Day Notice account paid 0.60% throughout the year from May 2013.

- The custodian based assets comprised of UK Government Treasury bills which offered better yields than the DMO for the same level of security and Commercial Paper (CP) issued by Network Rail Infrastructure (UK Government Guaranteed) and Transport for London CP to introduce greater diversification.

- Eight fixed term deals with three banks, with durations ranging from three weeks to five months. The investments were deposited with Lloyds Bank, Barclays Bank and The Royal Bank of Scotland.

3.2 The weighted average interest rate of return on the investments over the year was 0.48 per cent, with a total interest received of £1.30 million (compared with a weighted average of 0.90 per cent and a total interest £1.52 million for 2012/13). The rate fell due to maturity of higher rated loans and lower rates within the market.

3.3. The investment strategy for 2013/14 was to place cash investments with institutions as set out in the Treasury Management Strategy. The first objective was to place investments based on security and liquidity of the investments rather than to seek yield. Once security and liquidity criteria were satisfied, investments would then be placed taking yield into account.

3.4. The cash flow of capital receipts in 2013/14 is shown in the table below.

Capital Receipts 2013/14	**General Fund £'000**	**Housing £'000**	**Total £'000**
Opening Balance (01/04/2013)	**-**	**20,494**	**20,494**
Receipts Generated in Year	10,664	70,953	81,617
Receipts Pooled to Central Government under regulation	-	(5,616)	(5,616)
Cost of disposal	(168)	(442)	(610)
Deferred Costs of Disposal released	(97)	(183)	(280)
Receipts Used to Finance Capital Expenditure	(6,450)	(4,537)	(10,987)
Receipts applied to reduce long-term debt	(3,949)	(9,620)	(13,569)
Closing Balance (31/03/2014)	**-**	**71,049**	**71,049**

Borrowing

3.5. Total borrowings decreased by £11.56 million to £250.51 million due to maturing debt. The repayments were in line with the cash flow projection and paid by cash balances. No new borrowing was undertaken during the year.

3.6. The Council is currently maintaining an under-borrowed position[1]. This means that the capital borrowing need has not been fully funded by existing external loan debt and the balance is funded by cash reserves (Internal borrowing). This strategy is prudent as investment returns are low and counterparty risk is high.

3.7. General Fund debt - as measured by the Capital Financing Requirement (CFR) – reduced by £4.2million in year to £74.2 million at year end. A summary of the movement is shown in the table below.

[1] The Capital Financing Requirement (CFR) represents the underlying cumulative need to borrow for the past, present and future (up to 2 years in advance) amounts of debt needed to fund capital expenditure (net of receipts). Debt can be met not only from external loans but also by the temporary use of internally generated cash from revenue balances i.e. internal borrowing.

	2013/14 £m
Opening Capital Financing Requirement (CFR)	78.4
Revenue Repayment of Debt (MRP)	(1.5)
Annual (Surplus) in Capital Programme, after deferred costs of disposal.	(2.7)
Closing CFR	**74.2**

3.8. The HRA is responsible for servicing 82.9 per cent of the Council's external debt and the General Fund holds the remaining 17.1 per cent. The table below shows the details of the Council's external borrowing (as at 31 March 2014), split between the General Fund and HRA.

	General Fund £m	Average Interest rate	HRA £m	Average Interest rate	Total external borrowing £m	Combined Average Interest Rate
Total / average	42.79	5.42%	207.72	5.42%	250.51	5.42%

4. THE ECONOMY AND INTEREST RATES

4.1. Given the rapidly moving state of the economy, the details below focus on the last financial year, and it should be recognised that events have moved on since.

4.2 **US economy growth** was slow and stable despite a 16 day federal government shut down. The unemployment rate fell steadily throughout the period from 7.9% to end the period at 6.7%. The annual inflation rate moved between a range of 1.1% and 1.5%.

4.3 New Federal Reserve Chair Janet Yellen indicated that the US will be slow to raise interest rates due to low inflation and an above target unemployment rate. The Fed began to taper bond purchases by $10bn to $75bn in December. After three additional reductions the program currently stands at $45bn per month. The Fed reiterated that tapering is data dependant and they continue to watch economic indicators carefully.

4.4 **European economic austerity**, the main policy response, has devastating effects on the European area. The Eurozone experienced economic stagnation, mass unemployment, near deflation and anaemic GDP growth.

4.5 Greece, Ireland and Spain successfully issued debt on the capital markets but the underlying economic situation in many European countries is still far from normal.

4.6 The fallout from the situation in Crimea could be a headwind to the economic recovery in Europe as the area is heavily reliant upon imported Russian energy.

4.7 **UK Growth** was strong over the year. GDP growth was consistently around 0.8% each quarter with manufacturing proving a key driver. The National Institute of Economic and Social Research (NIESR) upgraded their forecast and predicated that the UK would be the fastest growth country in the G7. In February the annual rate of earnings growth matched the annual inflation (CPI) growth 1.7%. This is the first time that two measures have matched in four years and could signify a turning point in economic fortunes of households.

4.8 **UK CPI inflation** started the year at 2.4% before consistently falling and ending the year at 1.6%. RPI followed a similar downward trajectory.

4.9 **Gilt yields** increased throughout the year, as the expectations of rate rises were brought forward. Improved sentiment in the domestic economy and the gradual unwinding of US monetary stimulus (tapering) were the main drivers behind the steepening yield curve.

4.10 **The Bank of England Base Rate** was unchanged at 0.5% throughout the year while expectations of when the first increase would occur were steadily brought forward to the first quarter of 2015 from the second half of 2015. Governor Carney abandoned the concept of forward guidance, using unemployment rate of 7% as a threshold to discuss rate rises, just six months after introduction. The unemployment rate reached the threshold 7% much sooner than expected, leading the MPC to concentrate on a more broad range of indicators such as the output gap, income and spending. Deposit rates fell throughout the year as banks obtained funding from different sources.

4.11 **Risk premiums** stabilised and reduced slightly throughout the year. There were several upgrades to the credit ratings of sovereigns, particularly peripheral European Countries. Investors still remain cautious of longer-term commitment but overall there was an improvement in risk sentiment as major western economies continued on the path to economic recovery.

5. COMPLIANCE WITH TREASURY LIMITS AND PRUDENTIAL INDICATORS

5.1. During the financial year to March 2014, the Council operated within the treasury limits as set out in the Treasury Management Strategy (TMS). The outturn for the Treasury Management Prudential Indicators is shown in Appendix A.

6. CONSULTATION

6.1. N/a – for information only.

7. EQUALITY IMPLICATIONS

7.1. N/a – for information only.

8. LEGAL IMPLICATIONS

8.1. N/a – for information only.

9. FINANCIAL AND RESOURCES IMPLICATIONS

9.1. This report is wholly of a financial nature.

10. RISK MANAGEMENT

10.1. N/a – for information only.

11. PROCUREMENT AND IT STRATEGY IMPLICATIONS

11.1. N/a – for information only.

LOCAL GOVERNMENT ACT 2000
LIST OF BACKGROUND PAPERS USED IN PREPARING THIS REPORT

No.	Description of Background Papers	Name/Ext of holder of file/copy	Department/ Location
1.	Loans and Investments Ledger	Halfield Jackman Tri Borough Treasury Manager Tel 0207 641 4354	Tri Borough Treasury and Pensions 16th Floor, Westminster City Hall
2.	Treasury Management Strategy	Halfield Jackman Tri Borough Treasury Manager Tel 0207 641 4354	Tri Borough Treasury and Pensions 16th Floor, Westminster City Hall

LIST OF APPENDICES:
Appendix A – Treasury Management Prudential indicators

APPENDIX A

LBHF – TREASURY MANAGEMENT PRUDENTIAL INDICATORS 2013-14

Authorised Limit and Operational Boundary 31st March 13/14

Indicator	Approved Limit	Actual Debt	No. of days Limit Exceeded
Authorised Limit[2]	£345m	£250.51m	None
Operational Boundary[3]	£288m	£250.51m	None

Limits on Interest Rate Exposure

Interest Rate Exposure	Upper Limit	Lower Limit	Actual at 31 Mar 2014
Fixed Rate Debt	£320m	£0m	£250.51m
Variable Rate Debt	£64m	£0m	£0m

Maturity Structure of Borrowing

Maturity Structure of Borrowing	Upper Limit	Lower Limit	Actual at 31 Mar 2014
Under 1 year	15%	0%	1%
1 year to 2 years	15%	0%	6%
2 years to 5 years	60%	0%	9%
5 years to 10 years	75%	0%	9%
Over 10 years	100%	0%	75%

[2] The Authorised Limit is the maximum requirement for borrowing taking into account maturing debt, capital programme financing requirements and the ability to borrow in advance of need for up to two years ahead.

[3] The Operational Boundary is the expected normal upper requirement for borrowing in the year.