London Borough of Hammersmith & Fulham FULL COUNCIL 19 October 2016	
TREASURY OUTTURN REPORT 2015/16	
Report of the Cabinet Member for Finance - Councillor Max Schmid	
Open report	
Classification: For Information **Key Decision:** No	
Wards Affected: All	
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1. EXECUTIVE SUMMARY

1.1. This report presents the Council's Outturn Treasury Report for 2015/16 in accordance with the Council's treasury management practices.

2. RECOMMENDATIONS

2.1. That this report be noted.

3. REASONS FOR CONSIDERATION

3.1. The Code of Practice on Treasury Management 2011, adopted by the Chartered Institute of Public Finance and Accountancy and later by the Council, requires the following:

- Creation and maintenance of a treasury management policy statement which sets out the policies and objectives of the Council's treasury management activities. This was reported to the Cabinet in January 2012;
- Creation and maintenance of treasury management practices which set out the manner in which the Council will seek to achieve those policies and objectives;
- Receipt by the full Council of an annual treasury management strategy report for the year ahead and a mid-year review of the strategy;

- Receipt by the Cabinet Member for Finance and Strategy, the Audit and Transparency Committee and full Council of an annual review of the previous year (this report);
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and the execution and administration of treasury management decisions; and
- Delegation by the Council of the role of scrutinising of treasury management strategy and policy to a specific named body, which for this Council is the Audit and Transparency Committee.

4. INTRODUCTION AND BACKGROUND

4.1. Treasury management in this context is defined as:

"The management of the Council'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."[1]

4.2. This annual treasury report covers:

- the treasury position as at 31 March 2016;
- the borrowing strategy for 2015/16;
- the borrowing outturn for 2015/16;
- compliance with treasury limits and prudential indicators;
- investment strategy for 2015/16; and
- investment outturn for 2015/16.

5. CURRENT TREASURY POSITION

5.1. The Council's debt (all held with the Public Works Loan Board - PWLB) and investment positions at the beginning and end of the year were as follows:

£ million	31 March 2015 Principal	Rate/ Return at 31 March 2015	31 March 2016 Principal	Rate/ Return at 31 March 2016
Fixed Rate Borrowing				
General Fund (GF)	42.30	5.38%	39.62	5.11%
Housing Revenue Account (HRA)	205.30	5.38%	192.28	5.11%
Total / Weighted Average	**247.60**	**5.38%**	**231.90**	**5.11%**
Investments				
Total / Weighted Average	**359.78**	**0.50%**	**299.24**	**0.59%**

[1] Treasury Management Policy Statement adopted by Cabinet – 31 January 2012

5.2. The table below shows the allocation of interest paid and received during the year:

Fund	Interest Paid		Interest Received		Net £m
	Apportionment %	Amount £m	Apportionment %	Amount £m	
General Fund	17.1	(2.22)	62	1.25	(0.97)
Housing Revenue Account	82.9	(10.79)	25	0.48	(10.31)
other*	-	-	13	0.28	0.28
Total	100	(13.01)	100	2.01	(11.0)

* Other – Interest paid on balances held for Section 106 and other deposits.

5.3. Following the implementation of the self-financing initiative for housing, the Housing Revenue Account (HRA) is responsible for servicing 82.9% of the Council's external debt and the General Fund is responsible for the remainder.

5.4. **The Strategy for 2015/16**

5.5. The treasury strategy for 2015/16, approved by the Council on 2 February 2015, was based on the expectation that Bank rate would remain at the current level for most of the year.

5.6. Taking into account the worldwide economic climate it was considered appropriate to keep investments short-term and only invest with highly rated or UK Government backed institutions, resulting in relatively low returns compared to borrowing rates.

5.7. Due to the level of cash balances held by the Council (£360 million at 31 March 2015), it was anticipated that there would not be any need to borrow during 2015/16.

5.8. **Outturn for 2015/16**

5.9. Market expectations for an increase in Bank Rate moved during the year, starting at the third quarter of 2015, moving to the first quarter of 2016 and ending the year at the second quarter of 2017. Post year end the Base Rate has been cut to 0.25% and future increased pushed further back.

5.10. There has been some market volatility in equity prices during the year with corresponding impacts on bond prices and bond yields as investors sought safe havens. Bank Rate remained unchanged at 0.5%. Growth in the UK's Gross Domestic Product fell steadily from an annual rate of 2.9% in the first quarter of 2015 to 2.1% in the fourth quarter. Inflation forecasts have also been revised downwards.

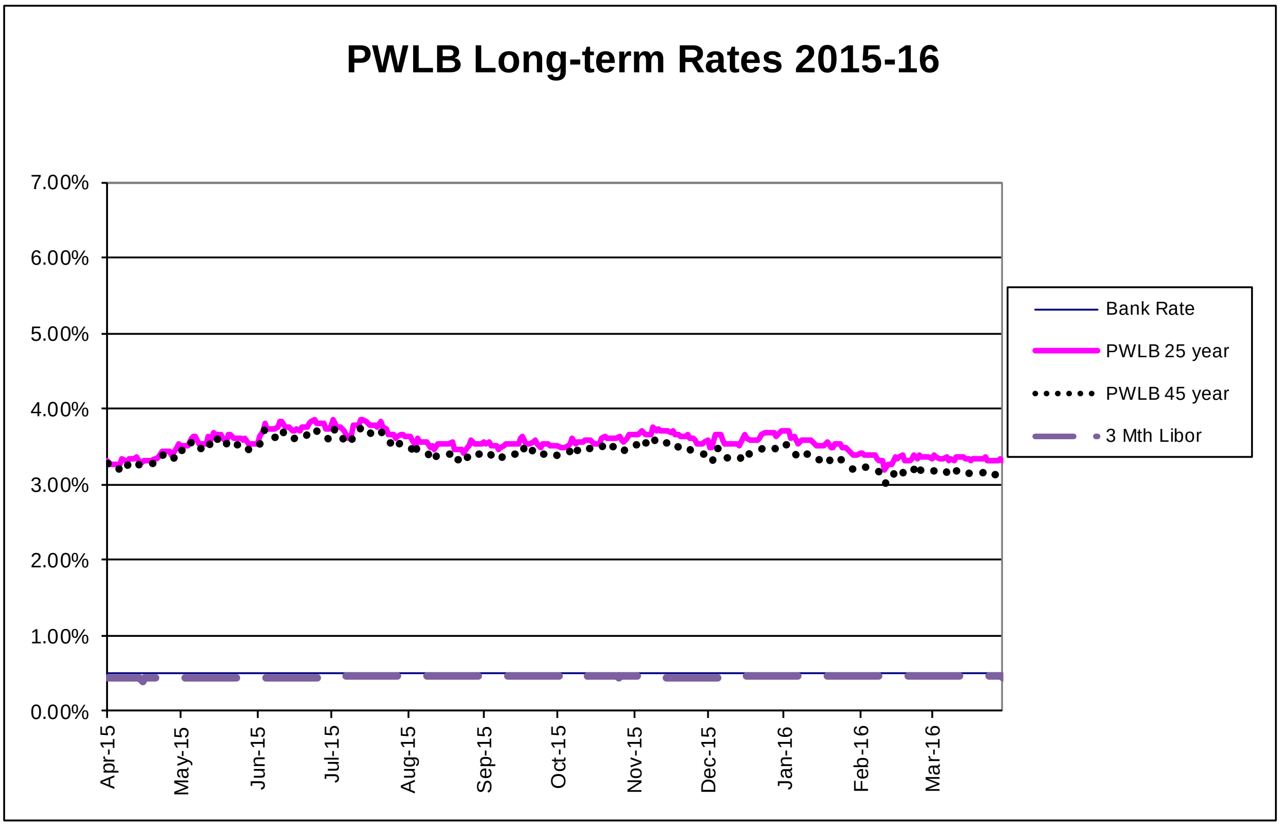
5.11. The European Central Bank commenced a quantitative easing programme in March purchasing sovereign bonds and securities from European institutions and national agencies at €60 billion a month. This is planned to continue until March 2017.

5.12. A majority Conservative government was elected in May 2015. The government has maintained the coalition's Government's fiscal policy but the recent downturn in expectations for economic growth has made it more difficult to return the public sector net borrowing to a balanced annual position.

5.13. **Treasury Borrowing**

5.14. No new long-term borrowing was undertaken during the year. Public Works Loans Board (PWLB) debt maturing during the year, which was not refinanced, totalled £15.7 million with an average nominal interest rate of 9.3 per cent. This resulted in a reduction in debt to £232 million and the average interest rates went from 5.38% to 5.11%.

5.15. The following graph shows the levels of Bank of England Bank rate, three month London Interbank Offer Rate (LIBOR), PWLB 25 and 45 year rates during the year:



5.16. The Bank of England Bank rate remained at its historic low of 0.5% throughout the year, for the seventh successive year. Deposit rates remained depressed during the whole year due to the ongoing weak expectation as to when the Bank rate would start rising.

5.17. In general, there has seen some movement of PWLB rates throughout the year but rates ended close to where they started.

5.18. **Housing Revenue Account (HRA) Self Financing**

5.19. Following the implementation of the self-financing initiative the HRA could potentially be in a position where it is internally borrowing from the general fund. In 2015/16 the HRA PWLB debt of £192 million has dropped below the HRA CFR of £205 million, which generates internal borrowing of £13 million. This difference does not, as yet, exceed the value of HRA working balances. As such, the HRA could be considered to be borrowing from itself. Moving forwards, a policy will need to be considered concerning the charging of interest in the event that the HRA is internally borrowing from the general fund. HRA reserves and working capital, in excess of the internal borrowing, represents cash balances on which interest is allocated from the general fund. As at 31 March 2016, the HRA held cash balances of £70.4 million.

5.20. **Capital Financing Requirement (CFR)**

5.21. As at 31 March 2016, the Council had an under-borrowed position[2]. This means that the capital borrowing need was not fully funded by existing external loan debt and the balance is funded by cash reserves (Internal borrowing).

The Closing Capital Financing Requirement analysed between General Fund and Housing Revenue Account.

£'000	31st March 2015 CFR	31st March 2015 DEBT	31st March 2016 CFR	31st March 2016 DEBT
GF CFR (Excluding DSG funded Schools Windows Borrowing)	45.182	-	44.179	-
GF CFR (DSG funded Schools Windows borrowing)	-	-	1.117	-
GF TOTAL	45.182	42.296	45.296	39.614
HRA TOTAL	204.846	205.302	204.846	192.282
TOTAL CFR/DEBT	**250.028**	**247.598**	**250.142**	**231.896**

NB: The 'headline' CFR shown above is the consistent with capital reports. The annual accounts disclose CFR of £267.58 million due to the inclusion of PFI, finance leases and deferred cost of disposal.

[2] 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.

5.22. **Annual Investment Strategy for 2015/16**

5.23. The 2015/16 Strategy was written with the knowledge that throughout the financial crisis institutions benefited from sovereign support but changes to the regulatory regime (Bail-in) meant support would be withdrawn and Credit ratings would fall at some point within the year. These changes did not reflect deterioration in the credit environment, more a realignment away from placing the burden on Governments (and taxpayers) on to institution bondholders.

5.24. Throughout the year the Council's strategy gradually moved away from fixed deposits with Banks to higher rated and more tradable investments like Government Treasury Bills (T/Bills), Supra-Nationals Banks and European Agencies, close to maturity Bonds, Certificates of Deposit and Commercial Paper.

- The Council strategy allowed investment in the following areas:
- An unlimited investment limit with the UK Government (DMO) deposits, UK gilts, Repos and T/Bills.
- Up to a maximum of £100 million per counterparty in Supra-national Banks, European Agencies and covered bonds debt on a buy to hold basis with maturity dates of up to five years. Transport for London(TfL) and Greater London Authority (GLA) for up to three years;
- No more than £25 million to be invested with any individual Money Market Fund.
- Any financial instrument held with a UK bank limited to £70 million depending on Credit rating and Government ownership above 25%.(A self-imposed limit of £50 million was implemented which has been further reduced temporarily to £25 million)
- Any financial instrument held with a Non-UK bank limited to £50 million.(A self-imposed limit of £30 million)

5.25. A small deposit was held in a National Westminster Bank call account to aid cash flow.

5.26. **Investment Outturn for 2015/16**

5.27. The investments outstanding at 31 March 2016 amounted to £299.24 million invested in short-term deposits. This compares with £359.78 million short-term investments at 1 April 2015.

5.28. The table below provides a breakdown of the cash deposits, together with comparisons from the previous year.

(£m)	**31/03/14**	**31/03/15**	**31/03/16**
Liquid Deposits	-	-	0.90
Money Market Funds	39.20	34.15	33.70
Notice Accounts	25.00	14.00	19.90
Custodian Held Assets	189.50	212.13	204.74
Term Deposits	66.50	99.50	40.00
Total	**320.20**	**359.78**	**299.24**

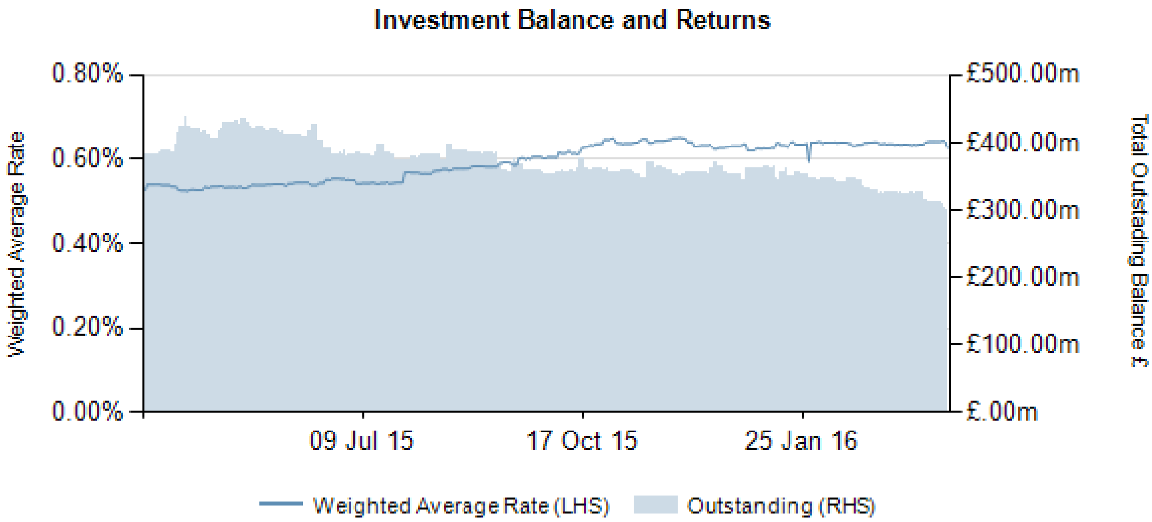
5.29. Investment balances reduced by £60 million during the year. The value of cash available for investment is impacted by:

- New borrowing and debt maturities,
- The capital programme – acquisitions and disposals
- Changes in reserves – additional reserves represent income banked for future use,
- Changes in debtors and creditors (working capital) – collecting debts more quickly increases cash balances while paying creditors more quickly leads to lower cash balances

5.30. Changes in cash are therefore an aggregation of many factors and are not equivalent to measuring the Council's overall surplus or deficit in the year. For example a reduction in cash due to paying creditors more quickly could be seen as socially responsible, where as an increase in cash due to delaying payments will be seen in a less favourable light. The main factors impacting on the reduction in investment balances in 2015-16 are:

- Debt maturities of £16 million
- Cash in transit of £31 million not banked relating to schools, which is reflected in higher debtor balances.
- Reduction in creditors for grants and provisions of £12 million (cash reduction)
- Other factors in aggregation – net cash reduction of £1 million.

5.31. The investments outstanding during the year together with the average return are shown in the diagram below. Cash balances varied between £435 million and £300 million reflecting the timing of the Council's income and expenditure. Balances tend to be highest in the June quarter due to grant and Council tax payments



5.32. The average return achieved on investments managed internally for the year was 0.59 per cent compared to the average 7 day money market rate (uncompounded) of 0.36 per cent. The total interest received of £2 million (compared with a weighted average of 0.50 per cent and a total interest £1.85 million for 2014/15). Interest rates remained low throughout the year; the Council follows a low risk strategy and does not seek potential higher returns which would increase counterparty risk.

6. COMPLIANCE WITH TREASURY LIMITS AND PRUDENTIAL INDICATORS

6.1. During the financial year the Council operated within the treasury limits set out in the Council's Treasury Policy Statement and Treasury Strategy Statement. The outturn for Treasury Management Prudential Indicators is shown in **appendix A**.

6.2. Non Treasury related Prudential Indicators are set and monitored as part of the Council's Budget process.

7. CONSULTATION

7.1. N/A – for information only.

8. EQUALITY IMPLICATIONS

8.1. N/A – for information only.

9. LEGAL IMPLICATIONS

9.1. N/A – for information only.

10. FINANCIAL AND RESOURCES IMPLICATIONS

10.1. N/A – for information only.

11. RISK MANAGEMENT

11.1. N/A – for information only.

12. PROCUREMENT AND IT STRATEGY IMPLICATIONS

12.1. N/A – for information only.

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

None.

LIST OF APPENDICES:

Appendix A – Treasury Management Prudential indicators

APPENDIX A

LBHF – TREASURY MANAGEMENT PRUDENTIAL INDICATORS 2015/16

Indicator	Approved Limit	Actual Debt	No. of days Limit Exceeded
Authorised Limit[3]	£345m		None
Operational Boundary[4]	£290m	£231.9m	None
Interest Rate Exposure	**Lower Limit**	**Upper Limit**	**Actual at 31 Mar 2016**
Fixed Rate Debt	£0m	£345m	£232m
Variable Rate Debt	£0m	£69m	£0m
Maturity Structure of Borrowing	**Lower Limit**	**Upper Limit**	**Actual at 31 Mar 2016**
Under 12 Months	0%	15%	3%
12 Mths to within 24 Mths	0%	15%	3%
24 Mths to within 5 years	0%	60%	11%
5 years to within 10 years	0%	75%	9%
Over 10 years	0%	100%	74%

[3] 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.

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