

**Treasury Management
2016-2017 Mid-Year Progress Report**

1. Contacts

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2. Executive Summary

The Chartered Institute of Public Finance and Accountancy's Treasury Management Code (CIPFA's TM Code) requires that Authorities report on the performance of the treasury management function at least twice yearly (mid-year and at year end). This report summarises performance for the six months to 30 September 2016.

Treasury management activities in the first half of 2016-17 were conducted in accordance with the Council's Treasury Management Strategy and achieved an overall return of 1.38% against a benchmark for other District Councils of 1.10%.

The largest contribution to this return was made by the Council's investment in the Local Authorities Property fund, and a further £5m investment was made on 29 September taking the Council's investment to the planned target of £10m.

3. Recommendation

- 3.1 **That the Cabinet considers and notes Chichester District Council's Treasury Management Mid-Year Progress Report for the six months to 30 September 2016.**

4. Background

- 4.1. The Chartered Institute of Public Finance and Accountancy's Treasury Management Code (CIPFA's TM Code) requires that Authorities report on the performance of the treasury management function at least twice yearly (mid-year and at year end). This report provides a summary of the Council's Treasury Management Activities for the half year to 31 September 2016.
- 4.2. The Authority's Treasury Management Strategy for 2016/17 was approved by full Council on 26 January 2016 and updated on 19 July. The Strategy is

available on the Council's internet site.

- 4.3. The Authority has continued to invest substantial sums of money and manage financial risks including the loss of invested funds and the revenue effect of changing interest rates. This report covers treasury activity and the associated monitoring and control of risk
- 4.4. A copy of this report was considered by the Corporate Governance & Audit Committee on 24 November 2016.

5. Outcomes to be Achieved

- 5.1. This report demonstrates treasury management activities in the first half of 2016-17 were conducted in accordance with the Council's Treasury Management Strategy and achieved an appropriate return given the Council's expressed risk appetite.
- 5.2. The Council continues to manage significant resources as part of its treasury management function. The funds managed increased in the first half of 2016-17 by £10.8m as shown in Exhibit 1, below.

Exhibit 1: Movement in treasury funds

Investments £000	Balance 01/04/2016	Movement	Balance 30/06/2016	Movement	Balance 30/09/16
Short term Investments (cash, call accounts, deposits)	29,465	3,450	32,915	(8,530)	24,385
Money Market Funds	4,420	(1,610)	2,810	7,690	10,500
Corporate Bonds	0	-	0	4,879	4,879
Total liquid investments	33,885	1,840	↑ 35,725	4,039	↑ 39,764
Long term Investments	10,000	-	10,000	-	10,000
Pooled funds – Local Authority Property fund	5,000	-	5,000	5,000	10,000
TOTAL INVESTMENTS	48,885	1,840	↑ 50,725	9,039	↑ 59,764

Short term investments include any investments that had an original period over greater than 1 year, but which will mature during 2016-17.

- 5.3. Reflecting the Council's Treasury Management Strategy, officers have continued to diversify into other forms of investment and/or higher yielding asset classes and the movement in investment balances reflects the following trends:
 - returns on Money Markets have proved more resilient to the August interest rate cut than those for new short term cash deposits

- short-term corporate bonds have been purchased where returns have exceeded available money market rates and where they meet our counterparty lending criteria
- a second investment of £5m was made in the local authority property fund in September 2016.

6. Externally Managed Funds

5.4. Following the Council's purchase of 1.6m units in the Local Authority' Property Fund (LAPF) in February 2016, a further 1,659,035 units were purchased on 29 September 2016, bringing the Council's total investment in this fund to £10m.

7. Borrowing Strategy During the Quarter

5.5. The Authority does not expect to borrow in 2016/17.

8. Investment Activity Benchmarking

5.6. The data below is presented in terms of the key objectives of public sector treasury management, Security, Liquidity and Yield for the previous four quarters.

Security

Measure	CDC Actuals				Non-met District average	Rating
	Qtr3 15-16	Qtr4 15.16	Qtr 1 16-17	Qtr 2 16-17		
Average Credit Score (time-weighted)	2.52	2.38	2.85	3.56	4.21	GREEN
Average Credit Rating (time weighted)	AA	AA+	AA	AA-	AA-	GREEN
Proportion Exposed to Bail-in (%)	29	18	19	41	66	GREEN

5.7. The Council's unsecured investments have been maintained above the target credit rating of A set out in Table 7 of its updated Treasury Management Strategy. The risk of bail-in continues to be managed by holding a relatively small proportion of investments with Banks and Building societies. The increase in holdings in the second quarter of 2016/17 is attributable to increased investments with Lloyds and Bank of Scotland (both with a minimum credit rating of 'A') to secure above market rate returns.

Liquidity

Measure	CDC Actuals				Non-met districts (average)	Rating
	Qtr3 15-16	Qtr4 15-16	Qtr 1 16-17	Qtr 2 16-17		

Proportion available within 7 days (%)	15	16	7	18	36	GREEN
Proportion available within 100 days (%)	53	39	49	44	61	GREEN
Average days to maturity	273	288	246	213	124	AMBER

- 5.8. The Council has a voluntary liquidity measure to maintain a minimum of £10m available within 3 months and this has been complied with throughout the period in question.
- 5.9. The relatively low proportion of funds available within 7 days continues to reflect the Council's active management of its investments to limit its exposure to bank bail-in, the majority of short term deposits being for periods of 1 to 6 months with Local Authorities or Bonds issued by large corporates.
- 5.10. The relatively high average days to maturity figure continues to reflect a number of longer term investments which generate additional returns for the Council's general fund.

Return

Measure	CDC Actuals				Non-met districts (average)	Rating
	Qtr3 15-16	Qtr4 15-16	Qtr 1 16-17	Qtr2 16-17		
Internal investment return %	0.79	0.84	0.82	0.82	0.64	GREEN
External funds – income return %	-	4.63	4.55	4.42	3.47	GREEN
External funds – capital gains/losses %	-	(7.20)	(10.13)	(9.16)	(1.50)	RED
Total treasury Investments – income return %	0.79	1.20	1.16	1.38	1.10	GREEN
Property – income return (investment Purchases only) % ¹	9.09	9.09	9.09	9.09		GREEN

¹ Note: This relates to properties managed directly by the Council's Estates Service.

- 5.11. The overall internal investment return on treasury investments continues to slightly exceed the target return for the year (0.75%), although officers expect overall returns to fall below this in the next six months due to the August reduction in the bank base rate.
- 5.12. The capital loss of 9.16% is due to the purchase of additional units in the Local Authority property fund on 29 September and represents the difference between the acquisition and sale price of fund units. This loss will only be charged to the Council's General Fund if the asset becomes impaired, is sold or is derecognised. At present this is not expected to occur as, although money can

be redeemed from this fund at short notice, the Council's intention is to hold them over the medium to long term.

- 5.13. The return for 2016-17 on our investment in the Local Authority Property Fund is shown below

	Dividend £	Dividend % (p.a)
April - June 2016	55,587	4.4
July - September 2016	52,884	4.2
Total for 6 months to September	108,471	4.3

- 5.14. Officers anticipate an investment outturn of £318,000 (4.2%) from this investment in 2016-17 and £425,000 for future financial periods.

9. Treasury Management Activity

- 5.15. Alongside the investment on the Local Authority Property Fund, the Council has also made a number of investments in corporate bonds issued by large corporates. These have been reported to Members of the Corporate Governance and Audit Committee via a weekly summary of investment activity undertaken.

- 5.16. The commencement of these investments has resulted in a change in the definition of 'principal' being adopted by officers to ensure that a prudent approach to the application of limits in the Council's Treasury Management Strategy is maintained.

- 5.17. Following investments in:

- Centrica Plc £1,000,000
- Scotland Gas Networks Plc £1,000,000
- Scottish Power UK plc £1,000,000

- 5.18. The definition of principal invested was amended to include any premiums paid on initial purchase. These sums are paid in addition to the nominal value of the bond as a result of acquiring a higher rate of return on the bond compared to other available investments and have ranged from £3,600 to £37,000 to date. These costs are included in any calculation of yield to maturity on the bond and covered by the interest received on the investment. This amended definition has been agreed with the Council's Treasury Management advisors and will be reflected in the Council's Treasury Management Strategy presented to Council in March 2017.

- 5.19. One investment during the period was made for a period that exceeded the maximum allowable period by 1 day. The was approved by the Director of Finance and Governance as no other suitable investment opportunities existed and the Council's money market funds was at the maximum available balance.

- 5.20. The Council's change of banker on 1 April 2016 continues to require the attention of Treasury staff. On the 2nd September the agreed balance 'sweeping' arrangements between the Council's accounts did not operate,

leading to the Council's creditors account being overdrawn by £6.3m overnight. National Westminster have acknowledged this was due to a failure of their systems and have confirmed no interest or other charges will be made to the Council as a result of this.

10. Other Treasury Management Indicators

5.21. The Authority also measures and manages its exposures to treasury management risks using the following indicators.

5.22. **Interest Rate Exposure:** This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the amount and proportion] of net principal invested are:

	2016/17	2017/18	2018/19
Upper limit on fixed interest rate exposure	£28m/40%	£24m/40%	£22m/40%
Actual (30 September 2016)	£10m/17%		
Upper limit on variable interest rate exposure	£70m/100%	£60m/100%	£55m/100%
Actual	£49.6m/83%		

5.23. Fixed rate investments and borrowings are those where the rate of interest is fixed for at least 12 months, measured from the start of the financial year or the transaction date if later. Instruments that mature during the financial year are classed as variable rate.

5.24. **Principal Sums Invested for Periods Longer than 364 days:** The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to final maturities beyond the period end will be:

	2016/17	2017/18	2018/19
Limit on principal invested beyond year end	£35m	£30m	£25m
Actual	£20m	£15m	£13m

5.25. **Liquidity:** The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three month period, without additional borrowing.

	Target	Actual 30/9/2016
Total cash available within three months (30 September 2016)	£10m	£20.7m

5.26. At present the Council is favouring shorter term investments due to flat interest yield curves for investments and also to maintain a potential for future investment in externally managed funds.

11. Investment Training

- 5.27. Training to help Members exercise proper oversight of Treasury Management activities is offered each year to all members. Members of the Corporate Governance and Audit Committee and the Cabinet are required to attend the next training session which is due to be held on 13 January 2017.

12. Resource and Legal Implications

- 5.28. Any investment interest received in the year is currently not used to help balance the revenue budget, but used to fund one off costs or towards funding capital projects. Any underperformance may therefore have an impact on the Council's overall funding position, but this is kept under review and reported to members as part of the budget process. Currently the approved capital programme remains fully funded.
- 5.29. The Council has complied with all the relevant statutory and regulatory requirements that limit the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management, means that, its capital expenditure is prudent, affordable and sustainable, and demonstrates a low risk approach

13. Other Implications

Crime and Disorder	None
Climate Change	None
Human Rights and Equality Impact	None
Safeguarding and Early Help	None

14. Appendix

- 5.30. Appendix - Benchmarking Definitions

15. Background Papers

- 5.31. Arlingclose Benchmarking Report for quarters 1 and 2 2016-17 (contains exempt information under Paragraph 3 (information relating to the financial or business affairs of any particular person (including the authority holding that information) of Part I of Schedule 12A to the Local Government Act 1972.

Appendix – Benchmarking Definitions

The benchmarking compares various measures of risk and return, which are calculated as follows:

Investment Value

For internal investments, the value is the sum initially invested. For external funds, the value is the fund's bid price on the quarter end date multiplied by the number of units held.

Rate of Return

For internal investments, the return is the effective interest rate, which is also the yield to maturity for bonds. For external funds (LAPF) this is measured on an offer-bid basis less transaction fees. For external funds the income only return excludes capital gains and losses.

Average returns are calculated by weighting the return of each investment by its value. All interest rates are quoted per annum.

Duration

This measure applies to internal investments only. This is the number of days to final maturity. For instant access money market funds, the number of days to final maturity is one.

Average duration is calculated by weighting the duration of each investment by its value. Higher numbers indicate higher risk.

Credit Risk

Each investment is assigned a credit score, based where possible on its average long-term credit rating from Fitch, Moody's and Standard & Poor's. This is converted to a number, so that AAA=1, AA+=2, etc. Higher numbers therefore indicate higher risk. Unrated local authorities are assigned a score equal to the average score of all rated local authorities.

Average credit risk is measured in two ways. The value-weighted average is calculated by weighting the credit score of each investment by its value. The time-weighted average is calculated by weighting the credit score of each investment by both its value and its time to final maturity. Higher numbers indicate higher risk.