CABINET

THURSDAY 30TH NOVEMBER 2017

REPORT OF THE PORTFOLIO HOLDER FOR ASSETS AND FINANCE

TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY MID-YEAR REVIEW REPORT 2017/18

EXEMPT INFORMATION

None

PURPOSE

To present to Members the Mid-year Review of the Treasury Management Strategy Statement and Annual Investment Strategy.

RECOMMENDATIONS

That Council be requested to accept the Treasury Management Strategy Statement and Annual Investment Strategy Mid-year Review Report 2017/18.

EXECUTIVE SUMMARY

This mid-year report has been prepared in compliance with CIPFA's Code of Practice, and covers the following

- An economic update for the first six months of 2017/18;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's Capital Position (Prudential Indicators);
- A review of the Council's investment portfolio for 2017/18;
- A review of the Council's borrowing strategy for 2017/18;
- A review of any debt rescheduling undertaken during 2017/18;
- A review of compliance with Treasury and Prudential Limits for 2017/18;
- Revised CIPFA codes and Markets in Financial Instruments Directive II (MIFID II)

The main issues for Members to note are:

1. The Council has complied with the professional codes, statutes and guidance.

2. There are no issues to report regarding non-compliance with the approved prudential indicators.

3. The investment portfolio yield for the first six months of the year is 0.52% (0.59% for the same period in 2016/17) compared to the 3 Month LIBID benchmark rate of 0.18% (0.38% for the same period in 2016/17).

The aim of this report is to inform Members of the treasury and investment management issues to enable all Members to have ownership and understanding when making decisions on Treasury Management matters. In order to facilitate this, training on Treasury Management issues was most recently delivered for Members in October 2015 and will be provided as and when required.

RESOURCE IMPLICATIONS

All financial resource implications are detailed in the body of this report which links to the Council's Medium Term Financial Strategy.

LEGAL/RISK IMPLICATIONS BACKGROUND

Risk is inherent in Treasury Management and as such a risk based approach has been adopted throughout the report with regard to Treasury Management processes.

SUSTAINABILITY IMPLICATIONS

None

BACKGROUND INFORMATION

The Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management (revised 2011) suggests that Members should be informed of Treasury Management activities at least twice a year, but preferably quarterly. This is the second monitoring report for 2017/18 presented to Members this year and therefore ensures the Council is embracing best practice. Cabinet also receives regular monitoring reports as part of the quarterly healthcheck on Treasury Management activities and risks.

The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the Treasury Management operations ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering maximising investment return.

The second main function of the Treasury Management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

Treasury Management 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*."

Introduction

The Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management (revised 2011) was adopted by this Council on 13th December 2012.

The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's Treasury Management activities.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
3. Receipt by the full Council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a **Mid-year Review Report** and an Annual Report (stewardship report) covering activities during the previous year.
4. Delegation by the Council of responsibilities for implementing and monitoring Treasury Management policies and practices and for the execution and administration of Treasury Management decisions.
5. Delegation by the Council of the role of scrutiny of Treasury Management strategy and policies to a specific named body. For this Council the delegated body is the Audit and Governance Committee.

This mid-year report has been prepared in compliance with CIPFA's Code of Practice, and covers the following:

- An economic update for the first part of the 2017/18 financial year;
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy;
- The Council's Capital Position (Prudential Indicators);
- A review of the Council's investment portfolio for 2017/18;
- A review of the Council's borrowing strategy for 2017/18;
- A review of any debt rescheduling undertaken during 2017/18;
- A review of compliance with Treasury and Prudential Limits for 2017/18.

1. Economic Update

1.1 UK

After the UK economy surprised on the upside with strong growth in 2016, growth in 2017 has been disappointingly weak; quarter 1 came in at only +0.3% (+1.7% y/y) and quarter 2 was +0.3% (+1.5% y/y) which meant that growth in the first half of 2017 was the slowest for the first half of any year since 2012. The main reason for this has been the sharp increase in inflation, caused by the devaluation of sterling after the referendum, feeding increases in the cost of imports into the economy. This has caused, in turn, a reduction in consumer disposable income and spending power and so the services sector of the economy, accounting for around 75% of GDP, has seen weak growth as consumers cut back on their expenditure.

However, more recently there have been encouraging statistics from the manufacturing sector which is seeing strong growth, particularly as a result of increased demand for exports. It has helped that growth in the EU, our main trading partner, has improved significantly over the last year. However, this sector only accounts for around 11% of GDP so expansion in this sector will have a much more muted effect on the average total GDP growth figure for the UK economy as a whole.

The Monetary Policy Committee (MPC) meeting of 14 September 2017 surprised markets and forecasters by suddenly switching to a much more aggressive tone in terms of its words around warning that Bank Rate will need to rise. The Bank of England Inflation Reports during 2017 have clearly flagged up that they expected CPI inflation to peak at just under 3% in 2017, before falling back to near to its target rate of 2% in two years' time. Inflation actually came in at 2.9% in August, (this data was released on 12 September), and so the Bank revised its forecast for the peak to over 3% at the 14 September meeting MPC. This marginal revision can hardly justify why the MPC became so aggressive with its wording; rather, the focus was on an emerging view that with unemployment falling to only 4.3%, the lowest level since 1975, and improvements in productivity being so weak, that the amount of spare capacity in the economy was significantly diminishing towards a point at which they now needed to take action. In addition, the MPC took a more tolerant view of low wage inflation as this now looks like a common factor in nearly all western economies as a result of increasing globalisation. This effectively means that the UK labour faces competition from overseas labour e.g. in outsourcing work to third world countries, and this therefore depresses the negotiating power of UK labour. However, the Bank was also concerned that the withdrawal of the UK from the EU would effectively lead to a decrease in such globalisation pressures in the UK, and so would be inflationary over the next few years.

The MPC increased Bank Rate to 0.5% in November. The big question is now whether this will be a one off increase or the start of a slow, but regular, increase in Bank Rate. As at the start of October, short sterling rates were indicating that financial markets do not expect a second increase until May 2018 with a third increase in November 2019. However, some forecasters are flagging up that they expect growth to improve significantly in 2017 and into 2018, as the fall in inflation will bring to an end the negative impact on consumer spending power while a strong export performance will compensate for weak services sector growth. If this scenario were to materialise, then the MPC would have added reason to embark on a series of slow but gradual increases in Bank Rate during 2018. While there is so much uncertainty around the Brexit negotiations, consumer confidence, and business confidence to spend on investing, it is far too early to be confident about how the next two years will pan out.

1.2 EU

Economic growth in the EU, (the UK's biggest trading partner), has been lacklustre for several years after the financial crisis despite the ECB eventually cutting its main rate to -0.4% and embarking on a massive programme of QE. However, growth picked up in 2016 and now looks to have gathered ongoing substantial strength and momentum thanks to this stimulus.

GDP growth was 0.5% in quarter 1 (2.0% y/y) and 0.6% in quarter (2.3% y/y). However, despite providing massive monetary stimulus, the European Central Bank is still struggling to get inflation up to its 2% target and in August inflation was 1.5%. It is therefore unlikely to start on an upswing in rates until possibly 2019.

1.3 USA

Growth in the American economy has been volatile in 2015 and 2016. 2017 is following that path again with quarter 1 coming in at only 1.2% but quarter 2 rebounding to 3.1%, resulting in an overall annualised figure of 2.1% for the first half year. Unemployment in the US has also fallen to the lowest level for many years, reaching 4.4%, while wage inflation pressures, and inflationary pressures in general, have been building. The Fed has started on a gradual upswing in rates with three increases since December 2016; and there could be one more rate rise in 2017 which would then lift the central rate to 1.25 – 1.50%. There could then be another four more increases in 2018. At its June meeting, the Fed strongly hinted that it would soon begin to unwind its $4.5 trillion balance sheet holdings of bonds and mortgage backed securities by reducing its reinvestment of maturing holdings.

1.4 Japan and China

Chinese economic growth has been weakening over successive years, despite repeated rounds of central bank stimulus; medium term risks are increasing. Major progress still needs to be made to eliminate excess industrial capacity and the stock of unsold property, and to address the level of non-performing loans in the banking and credit systems.
Japan is struggling to stimulate consistent significant growth and to get inflation up to its target of 2%, despite huge monetary and fiscal stimulus. It is also making little progress on fundamental reform of the economy.

1.5 Interest rate forecasts

The Council's treasury advisor, Link Asset Services (previously known as Capita Asset Services), has provided the following forecast:

	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Bank Rate	0.50%	0.50%	0.50%	0.50%	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%
5yr PWLB Rate	1.50%	1.60%	1.60%	1.70%	1.80%	1.80%	1.90%	1.90%	2.00%	2.10%	2.10%	2.20%	2.30%	2.30%
10yr PWLB View	2.10%	2.20%	2.30%	2.40%	2.40%	2.50%	2.60%	2.60%	2.70%	2.70%	2.80%	2.90%	2.90%	3.00%
25yr PWLB View	2.80%	2.90%	3.00%	3.00%	3.10%	3.10%	3.20%	3.20%	3.30%	3.40%	3.50%	3.50%	3.60%	3.60%
50yr PWLB Rate	2.50%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.00%	3.10%	3.20%	3.30%	3.30%	3.40%	3.40%

As expected, the Monetary Policy Committee (MPC) delivered a 0.25% increase in Bank Rate at its meeting on 2 November. This removed the emergency cut in August 2016 after the EU referendum. The MPC also gave forward guidance that they expected to increase Bank rate only twice more by 0.25% by 2020 to end at 1.00%. The Link Asset Services forecast as above includes increases in Bank Rate of 0.25% in November 2018, November 2019 and August 2020.

Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts (and MPC decisions) will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geopolitical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

The overall balance of risks to economic recovery in the UK is probably to the downside, particularly with the current level of uncertainty over the final terms of Brexit.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Bank of England monetary policy takes action too quickly over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- Geopolitical risks, especially North Korea, but also in Europe and the Middle East, which could lead to increasing safe haven flows.
- A resurgence of the Eurozone sovereign debt crisis, possibly Italy, due to its high level of government debt, low rate of economic growth and vulnerable banking system.
- Weak capitalisation of some European banks.
- The result of the October 2017 Austrian general election is likely to result in a strongly anti-immigrant coalition government. In addition, the new Czech prime minister is expected to be Andrej Babis who is strongly against EU migrant quotas and refugee policies. Both developments could provide major impetus to other, particularly former Communist bloc countries, to coalesce to create a major block to progress on EU integration and centralisation of EU policy. This, in turn, could spill over into impacting the Euro, EU financial policy and financial markets.
- Rising protectionism under President Trump
- A sharp Chinese downturn and its impact on emerging market countries

The potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- The Bank of England is too slow in its pace and strength of increases in Bank Rate and, therefore, allows inflation pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.
- UK inflation returning to sustained significantly higher levels causing an increase in the inflation premium inherent to gilt yields.
- The Fed causing a sudden shock in financial markets through misjudging the pace and strength of increases in its Fed.

Funds Rate and in the pace and strength of reversal of Quantitative Easing, which then leads to a fundamental reassessment by investors of the relative risks of holding bonds, as opposed to equities. This could lead to a major flight from bonds to equities and a sharp increase in bond yields in the US, which could then spill over into impacting bond yields around the world.

2. Treasury Management Strategy Statement and Annual Investment Strategy Update

The Treasury Management Strategy Statement (TMSS) for 2017/18 was approved by Council on 21st February 2017.

There are no policy changes to the TMSS; the details in this report update the position in the light of the updated economic position and budgetary changes already approved.

3. The Council's Capital Position (Prudential Indicators)

This part of the report is structured to update:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the prudential indicators and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

3.1 Prudential Indicator for Capital Expenditure

This table below shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the Budget.

Capital Expenditure by Service	2017/18 Original Programme	Budget B'fwd from 2016/17	Virements to Programme in Year	Total 2017/18 Budget	Actual Spend @ Period 6	Predicted Outturn	2017/18 Revised Estimate*
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
General Fund	2.421	2.731	0.245	5.397	0.760	3.236	4.511
HRA	16.413	9.575	-	25.988	4.918	11.961	25.983
Total	**18.834**	**12.306**	**0.245**	**31.385**	**5.678**	**15.197**	**30.494**

* Includes potential expenditure slippage into 2018/19

3.2 Changes to the Financing of the Capital Programme

The following table draws together the main strategy elements of the capital expenditure plans (above), highlighting the original supported and unsupported elements of the capital programme, and the expected financing arrangements of this capital expenditure. Any borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision).

This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

Capital Expenditure	**2017/18 Capital Programme £m**	**2017/18 Predicted Outturn £m**	**2017/18 Budget * £m**
Unsupported	4.972	0.100	8.214
Supported	13.862	15.097	23.171
Total spend	**18.834**	**15.197**	**31.385**
Financed by:			
Grants - Disabled Facilities	0.224	0.404	0.404
Coalfields Grant	-	0.092	0.222
Section 106's	0.100	0.239	0.239
GF Receipts	0.222	0.407	0.462
GF Reserve	0.180	0.259	0.519
Sale of Council House Receipts	0.114	0.204	0.341
HRA Receipts	0.500	0.513	0.513
HLF Assembly Rooms Lottery	0.316	0.215	0.344
Grants - Assembly Rooms (SLGF)	1.264	0.809	1.334
Public Contributions (Assembly Rooms)	-	-	0.025
HLF/SCC/Donation - Castle Mercian Trail	-	0.508	0.508
MRR	4.213	4.192	6.408
HRA 1-4-1 Replacements Receipts	0.650	0.879	0.879
HRA Reserve	5.009	2.564	7.161
HRA Regeneration Fund	1.070	3.566	3.566
HCA Grant	-	0.246	0.246
Total Financing	**13.862**	**15.097**	**23.171**
Borrowing need	**4.972**	**0.100**	**8.214**

* includes potential expenditure slippage into 2018/19

3.3 Changes to the Prudential Indicators for the Capital Financing Requirement, External Debt and the Operational Boundary

The following table shows the CFR, which is the underlying external need to incur borrowing for a capital purpose. It also shows the expected debt position over the period. This is termed the Operational Boundary.

Prudential Indicator – Capital Financing Requirement

We are on target to achieve the original forecast Capital Financing Requirement.

Prudential Indicator – the Operational Boundary for External Debt

Operational Boundary	2016/17 Outturn £m	2017/18 Capital Programme £m	2017/18 Projected Outturn £m	2017/18 Budget* £m
CFR – Non Housing	0.943	1.885	0.885	0.885
CFR – Housing	68.041	75.255	68.041	76.255
Total CFR	68.984	77.140	68.926	77.140
Net movement in CFR	**(0.058)**	**4.914**	**(0.058)**	**8.156**
Operational Boundary				
Expected Borrowing	63.060	65.060	63.060	63.060
Total debt 31 March	**63.060**	**65.060**	**63.060**	**63.060**

3.4 Limits to Borrowing Activity

The first key control over the treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for a capital purpose. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2017/18 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent.

Net Borrowing to CFR	2016/17 Outturn £m	2017/18 Original Estimate £m	2017/18 Projected Outturn £m	2017/18 Budget £m
Gross borrowing	63.060	65.060	63.060	63.060
Less investments	51.211	58.143	57.408	49.194
Net borrowing	11.849	6.917	5.653	13.867
CFR (year end position)	68.984	77.140	68.926	77.140

The Executive Director Corporate Services reports that no difficulties are envisaged for the current or future years in complying with this prudential indicator.

A further prudential indicator controls the overall level of borrowing. This is the Authorised Limit which represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Authorised Limit for External Debt	2017/18 Original Indicator	Current Position	2017/18 Revised Indicator
Borrowing	84.292	84.292	84.292
Total	84.292	84.292	84.292

4. Investment Portfolio 2017/18

In accordance with the Code, it is the Council's priority to ensure security of capital and liquidity and to obtain an appropriate level of return which is consistent with the Council's risk appetite. As set out in Section 1, it is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the current 0.50% Bank Rate. The continuing potential for a re-emergence of a Eurozone sovereign debt crisis, and its impact on banks, prompts a low risk and short-term strategy. Given this risk environment and the fact that increases in Bank Rate are likely to be gradual and unlikely to return to the levels seen in previous decades, investment returns are likely to remain low.

The Council held £64.5m of investments as at 30th September 2017 (£50.119m at 31st March 2017) and the investment portfolio yield for the first six months of the year is 0.52% against a benchmark of the 3 months LIBID of 0.18%. A full list of investments held as at 30th September 2017 is detailed in **APPENDIX 1**.

The Council's budgeted investment return for 2017/18 is £260k, and performance for the year is projected to be £26k below budget, due to continuing low interest rates.

CIPFA Benchmarking Club

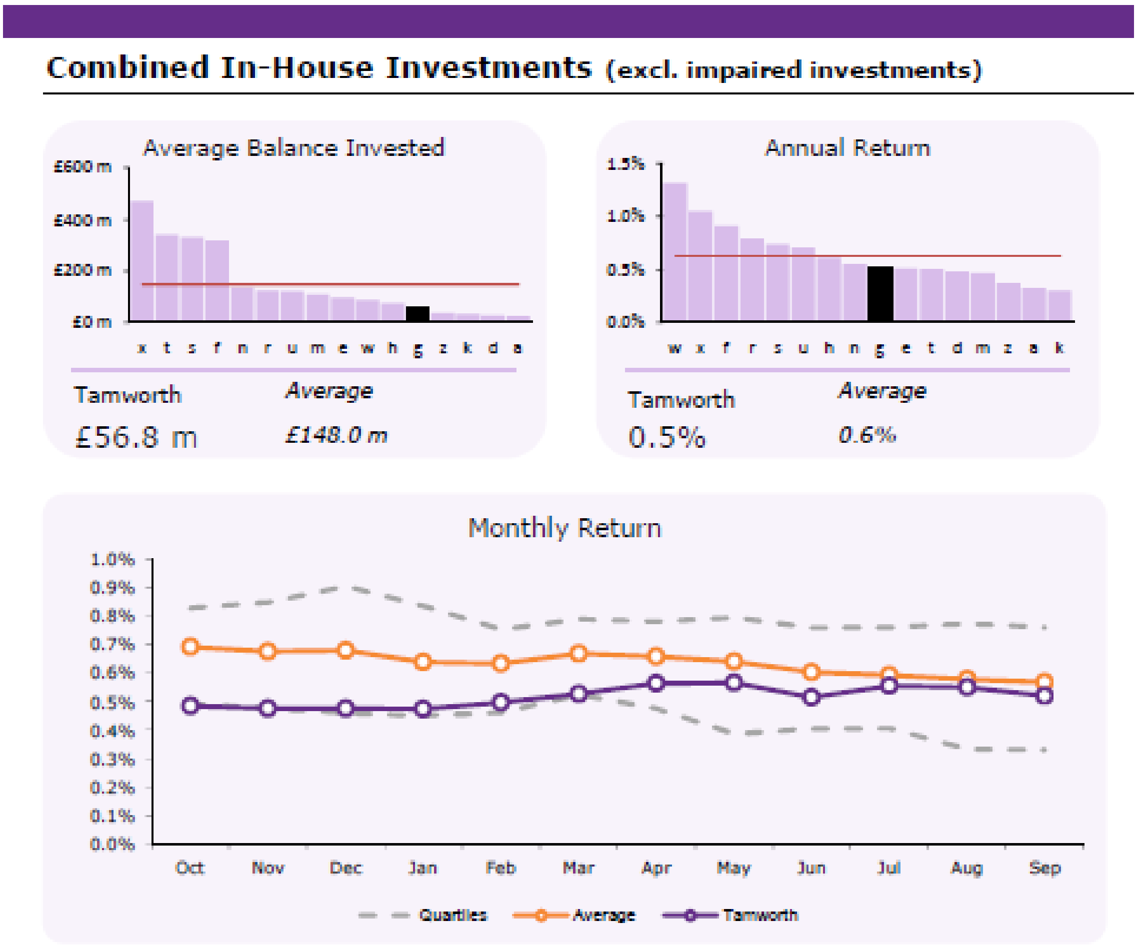
The Council is a member of the CIPFA Treasury Management Benchmarking Club which is a means to assess our performance over the year against other members. Our average return for In House Investments for the period October 2016 to September 2017 was 0.5% compared to the group average of 0.6% (information from CIPFA Benchmarking Report Q2 2017/18). This is considered to be a reasonable result in light of the current financial climate, our lower levels of deposits/funds and shorter investment time-lines due to Banking sector uncertainty, when compared to other Authorities.

This can be analysed further into the following categories:

Category	Average Balance Invested £m		Average Annual Return Received %	
	Tamworth Borough Council	CIPFA Benchmarking Club	Tamworth Borough Council	CIPFA Benchmarking Club
Fixed Investments (up to 30 days)	-	0.2	-	0.3
Fixed Investments (between 31 and 90 days)	-	1.2	-	0.3
Fixed Investments (between 91 and 364 days)	29.3	58.4	0.5	0.7
Fixed Investments (between 1 year and 3 years)	-	15.4	-	1.0
Fixed Investments (over 3 years)	-	12.3	-	2.2
Callable and Structured Deposits	-	11.3	-	1.7
Notice Accounts	12.0	22.4	0.7	0.4
Money Market Funds (Constant Net Asset Value)	9.5	24.2	0.2	0.3
Money Market Funds (Variable Net Asset Value)	-	29.2	-	0.6
DMADF	-	0.5	-	0.1
CDs, Gilts and Bonds	6.0	24.7	0.5	1.9
Average of all investments (Managed in House)	**56.8**	**148.0**	**0.5**	**0.6**

The data above and graphs below display that despite the Council being a small investor in the markets, performance is only marginally lower in those areas where both the Council and other member authorities invest.

The main variances arise from longer term fixed investments (in excess of 1 year) and instruments that the council do not currently get involved with i.e. Callable and Structured Deposits which are longer term deposits which (in line with our use of the Link Asset Services methodology and our approved specified limits in our Treasury Management strategy) are currently prohibited for Tamworth Borough Council and affirms our 'low appetite for risk' in the continuing unsettled markets.



Monthly Return (Oct 16 - Sept 17)													
	Oct	Nov	Dec	Jan	Feb	March	Apr	May	June	July	Aug	Sept	Year
Balance £'m	58.5	59.9	60.3	60.5	57.9	53.1	53.0	51.4	52.9	54.5	56.0	63.6	56.8
Interest £'k	24.1	23.4	24.3	24.3	22.1	23.8	24.5	24.7	22.3	25.6	26.1	27.1	292.3
Return	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.6%	0.6%	0.5%	0.6%	0.5%	0.5%	0.5%
Upper Quartile	0.8%	0.8%	0.9%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%	0.8%
Average	*0.7%*	*0.7%*	*0.7%*	*0.6%*	*0.6%*	*0.7%*	*0.7%*	*0.6%*	*0.6%*	*0.6%*	*0.6%*	*0.6%*	*0.6%*
Lower Quartile	0.5%	0.5%	0.5%	0.4%	0.5%	0.5%	0.5%	0.4%	0.4%	0.4%	0.3%	0.3%	0.5%
% Diff from Avg	-0.2%	-0.2%	-0.2%	-0.2%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	0.0%	0.0%	0.0%	-0.1%

Investment Counterparty Criteria

The current investment counterparty criteria selection approved in the TMSS and as approved by Council on the 21st February 2017 will meet the requirement of the Treasury Management function.

5. Borrowing

The Council's estimated revised capital financing requirement (CFR) for 2017/18 is £68.926m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. Table 3.4 shows the Council will have estimated borrowings of

£63.060m and has utilised £5.866m of cash flow funds in lieu of borrowing. This is a prudent and cost effective approach in the current economic climate but will require ongoing monitoring in the event that upside risk to gilt yields prevails.

In the first half of the year the Council had no PWLB debt maturing. The capital programme requires additional unsupported borrowing of £8.2m.

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is relatively high.

Use of internal funds is a more efficient use of resources as borrowing rates are significantly higher than investment returns. However, as and when resources are depleted or utilised, the opportunity to use internal balances will decrease and interest charges will increase.

Against this background and the risks within the economic forecast, caution will be adopted with the 2017/18 treasury operations. The Director of Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

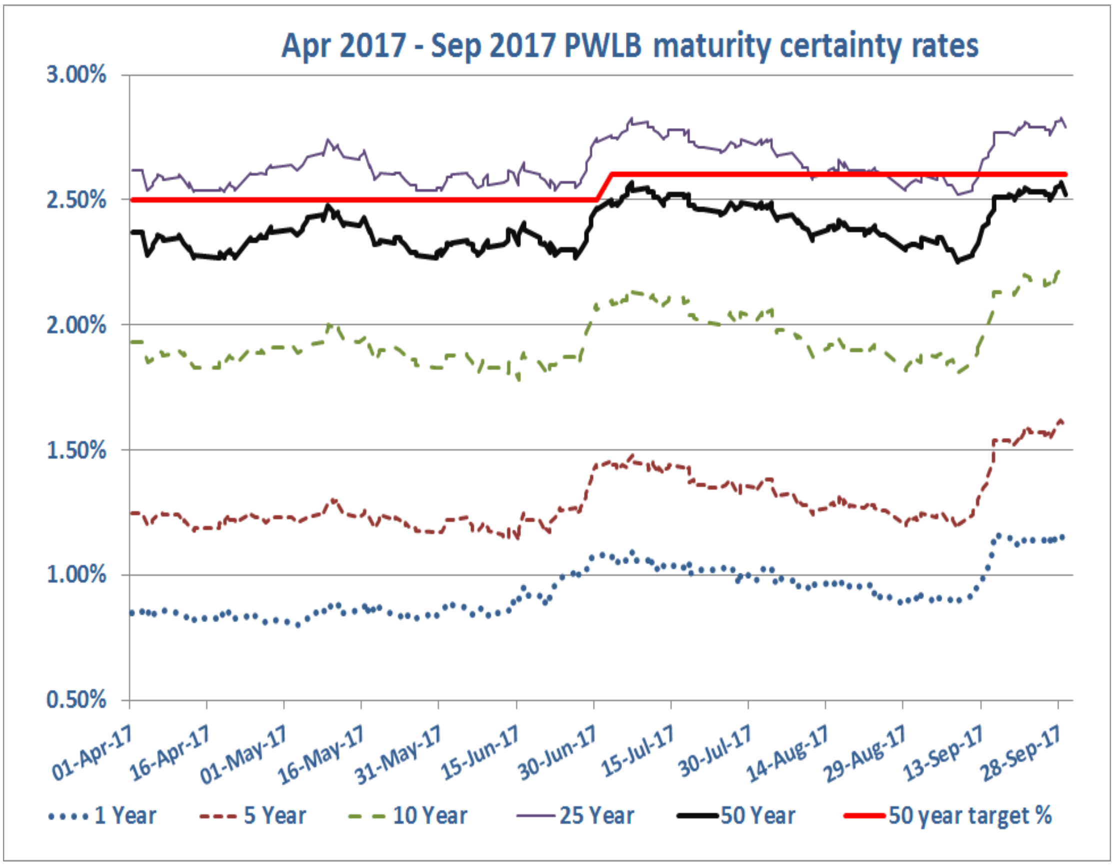
* *if it was felt that there was a significant risk of a sharp FALL in long and short term rates* (e.g. due to a marked increase of risks around recession or risks of deflation), then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

* *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast,* perhaps arising from a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still lower than they will be in the next few years.

Given the current economic forecasts for the coming years, it is unlikely that any additional borrowing will be undertaken during 2017/18.

The table and graph below show the movement in PWLB (Certainty Rates) for the first six months of the year to date:

PWLB certainty rates 1 April 2017 to 30 September 2017



	1 Year	5 Year	10 Year	25 Year	50 Year
Low	0.8	1.14	1.78	2.52	2.25
Date	03/05/2017	15/06/2017	15/06/2017	08/09/2017	08/09/2017
High	1.16	1.62	2.22	2.83	2.57
Date	15/09/2017	28/09/2017	28/09/2017	07/07/2017	07/07/2017
Average	0.9408	1.2981	1.9470	2.6475	2.3917

6. Debt Rescheduling

Debt rescheduling opportunities have been very limited in the current economic climate given the consequent structure of interest rates, and following the increase in the margin added to gilt yields which has impacted PWLB new borrowing rates since October 2010. No debt rescheduling has therefore been undertaken to date in the current financial year.

7. Revised CIPFA Codes and MIFID II

7.1 Revised CIPFA Codes

The Chartered Institute of Public Finance and Accountancy (CIPFA) is currently conducting an exercise to consult local authorities on revising the Treasury Management Code and Cross Sectoral Guidance Notes, and the Prudential Code. CIPFA is aiming to issue the revised codes during November.

A particular focus of this exercise is how to deal with local authority investments which are not treasury type investments e.g. by investing in purchasing property in order to generate income for the authority at a much higher level than can be attained by treasury investments. One recommendation is that local authorities should produce a new report to members to give a high level summary of the overall capital strategy and to enable members to see how the cash resources of the authority have been apportioned between treasury and non treasury investments. Officers are monitoring developments and will report to members when the new codes have been agreed and issued and on the likely impact on this authority.

7.2 MIFID II

MIFID is the EU legislation that regulates firms who provide services to clients linked to financial instruments and it is now being revised to strengthen consumer protection and improve the functioning of markets in light of the 2008 financial crisis.

The EU has now set a deadline of 3 January 2018 for the introduction of regulations under MIFID II. These regulations will govern the relationship that financial institutions conducting lending and borrowing transactions will have with local authorities from that date. This will have little effect on this authority apart from having to fill in forms sent by each institution dealing with this authority and for each type of investment instrument we use apart from for cash deposits with banks and building societies.

REPORT AUTHOR

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LIST OF BACKGROUND PAPERS

Background Papers -	*Local Government Act 2003*
	CIPFA Code of Practice on Treasury Management in Public Services 2011
	Annual Report on the Treasury Management Service and Actual Prudential Indicators 2016/17 –Council 12th September 2017
	Treasury Management Strategy & Prudential Indicators Report 2017/18 - Council 21st February 2017
	Budget & Medium Term Financial Strategy 2017/18 - Council 21st February 2017
	Financial Healthcheck Period 6, September 2017
	CIPFA Treasury Management Benchmarking Club Report Quarter 2, September 2017

APPENDICES

APPENDIX 1 Current Investment List

APPENDIX 1

Investments held as at 30th September 2017:

Borrower	Deposit £m	Rate %	From	To	Notice
Royal Bank of Scotland	2.00	0.65%	31-Jan-17	30-Jan-18	-
Lloyds Bank	2.00	0.55%	03-Apr-17	03-Oct-17	-
Lloyds Bank	2.00	0.55%	03-Apr-17	03-Oct-17	-
Royal Bank of Scotland	2.00	0.63%	05-Apr-17	04-Apr-18	-
Lloyds Bank	2.00	0.55%	10-Apr-17	10-Oct-17	-
Royal Bank of Scotland	2.00	0.67%	11-Apr-17	10-Apr-18	-
Sumitomo Mitsui Banking Corporation Europe Ltd	2.00	0.36%	18-Apr-17	18-Oct-17	-
Lloyds Bank	1.00	0.55%	28-Apr-17	30-Oct-17	-
Nationwide	1.00	0.37%	09-May-17	09-Nov-17	-
Nationwide	1.00	0.37%	31-May-17	30-Nov-17	-
Lloyds Bank	1.00	0.55%	01-Jun-17	01-Dec-17	-
Royal Bank Of Scotland	2.00	0.61%	05-Jun-17	25-May-18	-
Bank of Scotland	2.00	0.36%	30-Jun-17	02-Jan-18	-
Santander UK plc	8.00	0.70%	03-Jul-17	03-Jan-18	-
Royal Bank Of Scotland	2.00	0.6125%	10-Jul-17	29-Jun-18	-
Santander UK plc	2.00	0.70%	13-Jul-17	15-Jan-18	-
Barclays Bank	2.00	0.34%	17-Jul-17	17-Jan-18	-
Lloyds Bank	1.00	0.36%	09-Aug-17	09-Feb-18	-
Bank of Scotland	2.00	0.36%	10-Aug-17	12-Feb-18	-
Coventry BS	2.00	0.35%	05-Sep-17	05-Mar-18	-
Coventry BS	4.00	0.35%	13-Sep-17	13-Mar-18	-
Barclays Bank	3.00	0.31%	13-Sep-17	13-Mar-18	-
Nationwide	2.00	0.30%	13-Sep-17	13-Mar-18	-
Goldman Sachs International Bank	2.00	0.665%	15-Dec-16	-	180 day
Goldman Sachs International Bank	1.00	0.79%	10-Feb-17	-	180 day
Goldman Sachs International Bank	1.00	0.755%	06-Mar-17	-	180 day
Goldman Sachs International Bank	4.00	0.79%	13-Mar-17	-	180 day
Goldman Sachs International Bank	2.00	0.775%	05-Apr-17	-	180 day
MMF – PSDF	4.47	0.18*	-	-	On call
Total	**64.47**	**0.52 (avg)**	**-**	**-**	**-**

** Interest rate fluctuates daily dependant on the funds investment portfolio, rate quoted is approximate 7 day average.*

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