AGENDA ITEM No......4.:.......

NORTH LANARKSHIRE COUNCIL
REPORT

To: POLICY & RESOURCES (FINANCE & CUSTOMER SERVICES) SUB-COMMITTEE	Subject: TREASURY MANAGEMENT MONITORING REPORT PERIOD 1 OCTOBER TO 31 DECEMBER 2016
From: HEAD OF BUSINESS FOR FINANCIAL SOLUTIONS	
Date: 7 FEBRUARY 2016 Ref: PH/JQ/Q3	

1. Introduction

1.1 The purpose of this report is to inform on the quarterly activity (1 October 2016 to 31 December 2016) of the Council's loans and investment portfolio.

2. Background

2.1 The Council manages its treasury activities in line with the CIPFA Code "Treasury Management in the Public Services'. The Code requires the Council to produce reports on its Treasury Management policies, practices and activities on a regular and on-going basis. The Council fulfils these obligations in part by the preparation of a Treasury Management Monitoring report produced on a quarterly basis contained herein.

2.2 The Treasury activity undertaken in the third quarter of 2016/2017 reflects the key requirements of the Council's 2016/2017 Treasury Management Strategy, with the Public Works Loan Board and Long-term Money Market being the prime source of long-term funds. In terms of investment activity, this is conducted in accordance within the approved 2016/2017 investment strategy.

3. Quarterly Activity

3.1 Summary Position

3.1.1 The net overall borrowing position to 31 December 2016 is £732.3m, this representing an increase of almost £34.2m from the position at the 30 September 2016 with a detailed breakdown of the net cash movement shown in column (6) within Appendix 1.

3.2 Debt Restructuring

3.2.1 During the quarter under review, in conjunction with our Treasury advisors, we monitored the economic climate in relation to our financial targets and Treasury Management strategy. The interest rates prevailing throughout the period resulted in no beneficial opportunities for debt restructuring/rescheduling of the PWLB debt portfolio arising.

3.2.2 Further reports regarding future activity will be presented to Committee as appropriate.

3.3 Borrowing

3.3.1 At the end of the quarter, long term borrowing amounted to £481.6m which represented a fall of almost £6.2m as a result of £6.6m PWLB long term loans falling due for repayment, offset by the Council taking advantage of an interest free energy efficiency loan available from Salix Finance Ltd of £416K. This loan being for a period of 4 years representing the total long term borrowing that has been undertaken in the year to date. Internal cash balances and short term borrowing have been primarily used to meet the principal repayments, daily revenue account requirements and the capital financing requirement, in lieu of future borrowing for capital purposes. This approach adopted in light of interest rate expectations, management of carrying costs and the availability of short term borrowing at attractive rates.

3.3.2 During the quarter, short term borrowing rose by almost £13.5m as £51.9m of short term borrowing fell due for repayment with an additional £65.4m being sourced to meet these repayments and to replenish cash balances to appropriate levels to manage the associated investment, interest and liquidity risk. There was also a small decrease of £0.7m in the municipal bank balances available to the Council on a temporary borrowing basis at the 31 December 2016.

3.3.3 In September 2016, Greenfaulds High School was opened which was financed under a Subhubco/DBFM structure in conjunction with the private sector and the Scottish Futures Trust. This will be accounted for by the Council as credit arrangement and treated as a long term liability under the Prudential Code arrangements and £29.5m has therefore been included within the balances for long term liabilities at 31 December 2016.

3.3.4 During the quarter, there was also £1.3m in lease payments under existing finance lease and PPP obligations that fell due for repayment under the leasing arrangements in place, with long term liabilities amounting to £154.9m at 31 December 2016.

3.3.5 In October 2016, the Council was notified that it was successful in its application to the PWLB to access the certainty rate which allows a 20 basis point (bps) (0.2%) discount on loans from the Public Works Loan Board (PWLB) under the prudential borrowing regime for those principal local authorities providing improved information and transparency on their locally determined long-term borrowing and associated capital spending plans. This will provide the Council with an opportunity to borrow if required from the PWLB at more beneficial rates.

3.4 Short Term Investments

3.4.1 In the third quarter of 2016/2017, short-term investments of £152.2m in total were undertaken with approximately £154.0m of short-term investments maturing, the net effect of these transactions being a decrease of £1.8m in investment balances as shown in column 6 of the attached appendix 1.

3.4.2 At the end of the quarter the bank overdraft including cash in transit was almost £0.1m, representing a decrease of almost £2.4m compared to the total held at the end of the previous quarter as BACS receipts/payments were fully cleared by the 31 December 2016. This was due to the festive period scheduling with the balance of cash in transit and cheques unpresented balances offsetting each other.

3.4.3 The Council in line with the approved strategy to manage liquidity maintained a minimum balance of £3.0m available on an overnight basis (instant access) ensuring that the Council maintained the necessary prudent level of funds to meet all service objectives.

3.4.4 With the availability of the Funding for Lending scheme by the Government average short term rates continue to offer minimal returns with this scheme also skewing the relationship between the 7 day and 1 month LIBID (London Inter-bank Bid Rate) rate and generally available investment rates offered by financial institutions and money market funds. The Council continues to demonstrate good performance levels in investment activity, and continues to regularly outperform the 7 day and 1 month LIBID (London Inter-bank Bid Rate) rate.

3.4.5 The Treasury Management team continues to take a prudent approach to investing surplus funds in line with the approved 2016/2017 Investment Strategy the primary principle governing Council investment criteria being the security of the investment followed by ensuring sufficient liquidity in its investments.

3.5 Interest Rate Movements

3.5.1 At each of its meeting during this quarter the Monetary Policy Committee (MPC) decided to retain the Bank of England base rate at 0.25%. The likely path for the Bank Rate is weighted to the downside with a strong case for the Bank Rate to remain at 0.25%, but there still remains a 25% possibility of a drop to close to zero, with a very small chance of a reduction below zero.

3.5.2 The medium term outlook for the UK economy is dominated by the negotiations to leave the EU. The long-term position of the UK economy will be largely dependent on the agreements the government is able to secure with the EU and other countries. The global environment following the US election result and Brexit is also riddled with uncertainty, with repercussions for financial market volatility and long-term interest rates.

3.5.3 Financial markets currently have priced in stronger global growth following significant fiscal and monetary stimulus; the short term outlook for the global economy is indeed brighter than early 2016.

3.5.4 Economic data have presented a more positive picture for the post Referendum UK economy than predicted due to continued strong household spending. On the downside, the currency-led rise in CPI inflation (currently 1.6% year/year) will continue, breaching the target in 2017.

3.5.5 Following the reduction in the short term 7 day LIBID rate in the previous quarter, correlating closely to the 0.25% base rate reduction, there was very little movement in this rate, during the third quarter remaining around the 0.24% mark with it expected to remain on hold over the next few months.

3.5.6 Since the referendum result greater volatility has been demonstrated within the long term rates as there was an increase in demand for 'safe haven' UK gilts. Sporadic movements in supply and demand for UK gilts heavily influence gilt prices and yields, with corresponding movements up or down in the PWLB interest rates reflecting the perception of the improved stability or rising uncertainty in other non UK financial markets respectively.

3.5.7 During the quarter under review the average PWLB 10 year borrowing rate was 2.29% with a 0.81% spread between the highest and lowest interest rate available throughout the quarter which were 2.55% and 1.74% respectively. This represents a rise of approximately 0.49% from an average of 1.80% in the preceding 3 months. A similar trend is also being shown across longer borrowing periods over 20 years up to 50 years.

3.5.8 Although the lower long term borrowing rates in their own right appear attractive an internal review of the borrowing strategy still supports the Council's current strategy to utilise internal balances and access shorter term borrowing at attractive low rates. The Treasury Management Section will continue to monitor financial and economic policy and their impact upon the Council's investment and borrowing activity.

4. <u>The Prudential Code for Capital Finance in Local Authorities</u>

4.1 The Local Government in Scotland Act 2003 requires the Council to undertake its Treasury activities with regard to the Prudential Code for Capital Finance in Local Authorities.

4.2 Committee, at its meeting on 24 February 2016, approved a report titled, "Treasury Management Strategy 2016/2017 and Treasury and Prudential Indicators 2016/2017 to 2018/2019". This report detailed a variety of mandatory and local indicators aimed at assisting members to determine that proposed capital investment levels and treasury management decisions satisfied the key requirements of affordability, prudence and sustainability. Performance against key prudential indicators for 2016/2017 is detailed within Appendix 2.

4.3 Committee will wish to note the following salient points:-

(i) Indicator 1(a) illustrates that capital expenditure is in line with original estimates although the resource mix to finance the projects is different from the sources anticipated. This is monitored in detail as part of the Council's capital programme reporting mechanisms. The capital expenditure being met by an increase in capital contributions from revenue sources, capital receipts and cash grants with a reduction in the anticipated borrowing requirement for 16/17.

(ii) The Prudential Code requires the Council's capital investment to be affordable and prudent. To demonstrate this, a Prudential Margin (the need to borrow versus actual borrowing) is calculated. Indicator 1(b) demonstrates a healthy prudential margin at the 31 December 2016. The timing and profile of external borrowing to replenish cash reserves and balances having been managed giving full consideration to liquidity, interest rate and refinancing risk whilst minimising the potential carrying costs.

(iii) Indicator 2 illustrates that both the overall authorised and operational borrowing limits for borrowing and long term liabilities have not been exceeded, with the maximum borrowing undertaken within the period being well below the approved boundaries.

(iv) Indicator 3(a) sets upper limits on the Council's exposure to the effects of interest rate changes by setting limits for each category of debt held (fixed or variable rate) which subsequently limits the Council's interest payable that is fixed or variable. During the third quarter of 2016/2017, the actual levels remained below the limits for the fixed and variable interest rate exposure limits.

(v) Indicator 3(b) highlights a projected loan charge saving of almost £1.0m compared to the prudential estimates for 2016/2017 taking into account both the treasury management activity and the annuity based loans fund accounting requirements.

(vi) A treasury management saving of £1.8m reflecting the cashflow management techniques adopted, directing the timing of new borrowing, managing investment security, liquidity and interest rate risk and the identification of short term borrowing opportunities. This resulting in reduced loans fund interest payments and expenses with a minor reduction in investment income expected as financial institutions lower the investment rates offered following the reduction in the official base rate.

(vii) Per the annuity based loans fund accounting requirements the schedule for capital advances repayment has been re-calculated to reflect the savings in interest payments and the corresponding reduction in the loans fund interest annuity rate. Due to the intricacies of the annuity accounting model this results in an increase of £0.8m in capital advances due for repayment by services from their revenue resources.

(viii) Indicator 3(c) relates to the level of fixed debt due to mature within time periods. The level of debt maturing remains within the upper limits set for each category at the beginning of the financial year.

4.4 The prudential indicators have remained in accordance with those approved by Committee on 24 February 2016.

5. Recommendation

5.1 It is recommended that Committee:

(i) Notes the treasury management activity for the quarter ended 31 December 2016, including the positive performance against the key prudential indicators.

HEAD OF BUSINESS FOR FINANCIAL SOLUTIONS

Members seeking further information on the contents of this report are asked to contact Joseph Quinn, Finance Manager (Systems and Treasury Management) on telephone number 01698 302061.

LOANS , LONG TERM LIABILITIES & INVESTMENTS AS AT 31 DECEMBER, 2016

APPENDIX 1

	BALANCE 1-Oct-16 (1)	DEBT RESTRUCTURING		NEW BORROWING / LONG-TERM LIABILITIES (4)	PRINCIPAL REPAYMENTS (5)	NET CASH MOVEMENTS (6)	BALANCE 31-Dec-16 (7)
		EARLY REDEMPTION (2)	REFINANCING (3)				
LONG-TERM LOANS							
PWLB	389,761,304	0	0	0	(6,581,092)	(6,581,092)	383,180,212
MONEY MARKET LOANS	98,000,000	0	0	0	0	0	98,000,000
ENERGY EFFICIENCY LOAN	0			416,364	0	416,364	416,364
	487,761,304	0	0	416,364	(6,581,092)	(6,164,728)	481,596,576
SHORT-TERM LOANS							
TEMPORARY	80,380,000	0	0	65,380,000	(51,880,000)	13,500,000	93,880,000
MUNICIPAL BANK	43,167,509	0	0	0	(668,074)	(668,074)	42,499,435
INTERNAL LOANS	6,280	0	0	0	0	0	6,280
	123,553,789	0	0	65,380,000	(52,548,074)	12,831,926	136,385,715
LONG -TERM LIABILITIES							
FINANCE LEASE OBLIGATIONS	2,542,971	0	0	0	0	0	2,542,971
PPP LONG TERM LIABILITY	124,114,500	0	0	29,503,000	(1,261,250)	28,241,750	152,356,250
	126,657,471	0	0	29,503,000	(1,261,250)	28,241,750	154,899,221
TOTAL EXTERNAL DEBT	**737,972,565**	**0**	**0**	**95,299,364**	**(60,390,416)**	**34,908,948**	**772,881,513**
INVESTMENTS							
SOUTHWEST HUBCO	842,967	0	0	0	0	29,477	872,444
BANKS & OTHER FINANCIAL INSTITUTIONS	41,610,000	0	0	0	0	(1,769,500)	39,840,500
BANK OVERDRAFT INCL CASH IN TRANSIT	(2,528,836)	0	0	0	0	2,425,913	(102,923)
CASH & CASH EQUIVALENTS	**39,924,131**	**0**	**0**	**0**	**0**	**685,890**	**40,610,021**
NET BORROWING	**698,048,434**	**0**	**0**	**95,299,364**	**(60,390,416)**	**34,223,058**	**732,271,492**

Prudential Code for Capital Finance in Local Authorities

1. Capital Expenditure, Capital Financing Requirement and Prudential Margin

(a) Capital Expenditure

	Initial Estimate 2016/2017 (£m)	Projected Outturn 2016/2017 (£m)
Total spend : Capital Expenditure	118.7	118.7
Greenfaulds Subhubco/DBFM	29.5	29.5
Total Capital Investment	**148.2**	**148.2**
Financed By:		
Borrowing	55.4	35.7
Credit Arrangement : Greenfaulds	29.5	29.5
Capital Receipts	4.0	11.0
Cash Grants	33.4	39.7
Capital from Current Revenue	25.9	32.3

(b) Prudential Margin Calculation

	Initial Estimate 2016/2017 (£m)	Projected Outturn 2016/2017 (£m)
Capital Financing Requirement	895.4	895.6
Gross Borrowing	834.7	801.1
Prudential Margin	60.7	94.5

2) Authorised Limit and Operational Boundary

	Initial Authorised Limit 2016/2017 (£m)	Initial Operational Boundary 2016/2017 (£m)	Maximum Borrowing Level Q3 2016/2017 (£m)
Borrowing	850.0	840.0	629.9
Other Long-term Liabilities	160.0	160.0	154.9
Totals	1,010.0	1,000.0	784.8

3. Treasury Management Indicators

a) Interest Rate Exposures

	Upper Limits 2016/2017 (%)	Position as at 31/12/16 (£000s)
Fixed Interest Rates	110.00%	86.20%
Variable Interest Rates	30.00%	13.80%

b) Loans Fund Revenue Account

	Initial Estimate 2016/2017 (£m)	Projected Outturn 2016/2017 (£m)	Variance (£m)	%tage
Loans Fund Interest Payments	30.34	28.53	-1.81	-5.97%
Loans Fund Expenses	0.33	0.30	0.03	9.09%
Total Loans Interest Payments & Expenses	**30.67**	**28.83**	**-1.84**	**-6.00%**
Loans Funds Investment Income	0.20	0.14	-0.06	-30.00%
Total Loans Fund Interest Payments Investment Income & Expenses	**30.47**	**28.69**	**-1.78**	**-5.85%**
Capital Advances Repayments	**28.40**	**29.20**	**0.80**	**2.82%**
Total Loan Charges	**58.87**	**57.89**	**-0.98**	**-1.67%**

c) Maturity Structure of Borrowing

	<12months	12 months to 2 years	2 to 5 years	5 to 10 years	10 to 20 years	20 to 40 years	>40 years
Upper Limit maturing :Fixed Rate Debt	20.00%	15.00%	20.00%	30.00%	30.00%	40.00%	30.00%
Lower Limit maturing :Fixed Rate Debt	0.00%	0.00%	5.00%	5.00%	5.00%	10.00%	5.00%
Maturity structure at the start of Q3	5.80%	4.42%	8.25%	23.47%	12.13%	36.16%	9.77%
Maturity structure at the end of Q3	5.50%	3.28%	9.36%	22.79%	12.34%	36.79%	9.94%