*PART 1 – PUBLIC DOCUMENT *DRAFT*	AGENDA ITEM No. **16**

TITLE OF REPORT: TREASURY MANAGEMENT FIRST QUARTER REPORT 2014/15

REPORT OF THE STRATEGIC DIRECTOR OF FINANCE, POLICY & GOVERNANCE

Note: This report is in a draft format prior to presentation to Cabinet on 23 September 2014

1. SUMMARY

1.1 To inform Cabinet of the Treasury Management activities in the first quarter 2014/15 to the end of June.

1.2 To inform Cabinet of the performance against the Prudential and Treasury indicators.

2. RECOMMENDATIONS

2.1 Cabinet is asked to note the position of Treasury Management activity as at the end of June 2014.

3. REASONS FOR RECOMMENDATIONS

3.1 To ensure the Council's continued compliance with CIPFA's code of practice on Treasury Management and the Local Government Act 2003 and that the Council manages its exposure to interest and capital risk.

4. ALTERNATIVE OPTIONS CONSIDERED

4.1 Considerations for the Treasury Strategy can be summarised under the headings; Security, Liquidity and Yield. These considerations are listed in order of importance but all have an influence on the adopted Strategy. In particular the yield from investments is an important income stream for the general fund. The current strategy enables an above average yield compared to other Herts authorities of approximately £0.49M of interest in the financial year. Our Treasury advisors from Capita Asset Services Ltd promote a more risk averse approach that would not currently allow investment with most Building Societies. This would result in a lower yield but the option has been dismissed on the basis of Members' appetite for risk and the impact on the general fund.

5. CONSULTATION WITH EXTERNAL ORGANISATIONS AND WARD MEMBERS

5.1 There is ongoing dialogue with the Authority's Cash Managers (Sterling and Tradition) and regular meetings with Treasury advisors (Sector).

6. FORWARD PLAN

6.1 This Report does contain a recommendation on a key decision that was first included in the Forward Plan on 30 June 2014.

7. BACKGROUND

7.1 Members adopted the 2013/14 Treasury Strategy at the meeting of full Council on the 13 February 2014. The Treasury Strategy Statement contained no major changes from the 2013/14 Strategy.

7.2 Capita Asset Services Ltd were first contracted to provide Treasury advice for the financial year 2012/13 and this arrangement has been continued for 2014/15. The service includes regular updates on economic and political changes which may impact on the Council's borrowing and investment strategies, advice on rescheduling, information and prudent parameters in respect of investment counterparty creditworthiness, document templates, access to technical updates and to the Technical Advisory Group.

8. ISSUES

8.1 Appendix A provides the Treasury Management update at the end of the first quarter. This document contains economic background, an interest rate forecast and summary outlook provided by Capita for background context to Treasury activities. The remainder of the document contains an update on the Council's investment strategy.

8.2 In summary, the Council has operated within the treasury and prudential indicators set out in the Treasury Management Strategy Statement and in compliance with the Treasury Management Practices with the exception of exceeding the £9M investment limit with Lloyds bank for a small number of days. The maximum of funds held with Lloyds at any one time during the first quarter was £11.3M. The majority of these funds were held in the Lloyds current account and so could have been accessed at anytime. However, to be compliant with the Strategy total funds held with Lloyds should be maintained at no more than £9million.

8.3 The Council generated £0.128M of interest during the first quarter of 2014/15. The average interest rate agreed on new deals during the quarter by the cash managers (Sterling and Tradition) was 1.25 per cent. The average interest rates on all outstanding investments, (including in house deals) at the 30th June was 1.57 per cent.

8.4 The Council's activities expose it to a variety of risks (credit, liquidity and market). The Treasury Strategy sets out the Authority's appetite for the level of exposure to these risks. Firstly, **Credit Risk** – The possibility that other parties fail to pay amounts due to the Authority.

8.5 The Council's counterparty list comprises mostly UK building societies and UK banks with a Fitch (a credit rating agency) credit rating greater than BBB but also includes other Local Authorities and Public Corporations.

8.6 It continues to prove challenging to find counterparties willing to pay a reasonable return on cash investments, either long or short term. Capita advised this could be in part due to the Government scheme to lend money to counter-parties who are willing to then lend to businesses (this "funding for lending" scheme has been extended to

January 2015). As a result there is less of a demand for Local Authority funds. This issue is expected to continue during 2014/15 and is coupled with a reduction in the rate the Council will receive on the Nat West call account (for short term deposits). The rate of interest on this account for the majority of 2012/13 was 0.9 per cent. This was reduced to 0.5 per cent in March 2013 and reduced again in May 2014 to 0.25 per cent.

8.7 The Council's new general current account with Lloyds provides an interest rate of 0.4 per cent (the previous general current account with HSBC did not pay any interest).This rate is very competitive and means it is cost effective to keep a substantial balance in the current account rather than place funds with other institutions.

8.8 **Liquidity Risk –** the possibility that the Authority may not have funds available to meet its commitments to make payments.

8.9 Investments are split between two Cash Managers and the In-House team. The In-House investments cover the day to day cash flow activity of the Council whilst the Cash Managers' investments take advantage of higher long term interest rates when they become available. The Council had to borrow £0.57M for one day in April to cover a shortfall in cashflow. The shortfall occurred as £8.7M of expenditure (County Precept, Benefits and Salaries) was paid on the 14^{th} whilst £4.2M of income (Housing Subsidy Grant and Council Tax) was not received until the 15th. Interest paid on this loan was £9.53.

8.10 **Market Risk** - the possibility that financial loss might arise as a result of changes in interest rates.

8.11 Investing long term (greater than one year) currently achieves higher interest rates than short term deals. The risk of long term deals are two fold:

(i) The longer the time period the longer the investment is exposed to default.
(ii) If the investment has a fixed interest rate, interest rates could rise and the potential to invest at a higher rate will be lost until the investment matures.

8.12 Members have indicated that they are prepared to accept this risk within the limits expressed in the Treasury Strategy which allows no more than £20M (out of a total of just over £41M) to be invested for longer than 364 days at any one time. At the end of the first quarter the Council had £9.25M invested for longer than 364 days. Two deals were placed during the quarter for longer than one year totalling £3.0M.

9. LEGAL IMPLICATIONS

9.1 The Cabinet has a responsibility to keep under review the budget of the Council and any other matter having substantial implications for the financial resources of the Council.

9.2 Section 151 of the Local Government Act 1972 states that:
".every local authority shall make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs."

9.3 The Prudential Indicators comply with the Local Government Act 2003.

10. FINANCIAL IMPLICATIONS

10.1 The amount of investment interest expected to be generated during the year is £0.49M. This is approximately in line with the original budget figure of £0.48M.

10.2 Potential options for inclusion in the Treasury Strategy are considered as and when identified. Any proposals to amend the Strategy are reported to Full Council, via Cabinet, for approval.

11. RISK IMPLICATIONS

11.1 Risks associated with treasury management and procedures to minimise risk are outlined in the Treasury Management Practices document, TMP1, which was adopted by Cabinet in July 2003. The risk on the General Fund of a fall of investment interest below the budgeted level is dependant on banks and building societies need for borrowing. The introduction of the Funding for Lending Scheme, which allows financial institutions access to low cost funding from Government for an extended period has impacted on their need to borrow and the rates at which they are prepared to borrow.

12. EQUALITIES IMPLICATIONS

12.1 The Equality Act 2010 came into force on the 1 October 2010, a major piece of legislation. The Act also created a new Public Sector Equality Duty, which came into force on the 5 April 2011. There is a General duty, described in 12.2, that public bodies must meet, underpinned by more specific duties which are designed to help meet them.

12.2 In line with the Public Sector Equality Duty, public bodies must, in the exercise of its functions, give **due regard** to the need to eliminate discrimination, harassment, victimisation, to advance equality of opportunity and foster good relations between those who share a protected characteristic and those who do not.

12.3 There are no equalities implications arising from this report.

13. SOCIAL VALUE IMPLICATIONS

13.1 There are no social value implications arising from this report.

14. HUMAN RESOURCE IMPLICATIONS

14.1 There are no direct human resource or equality implications.

15. APPENDICES

15.1 Appendix A - Annual Treasury Management Update June 2014.

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17. BACKGROUND PAPERS

Treasury Strategy 2014/15
CIPFA Prudential Code for Capital Finance in Local Authorities