**Annex A**

CITY OF YORK COUNCIL

**Executive** **30 June 2016**

**Report of the Director of Customer and Business Support Services (Portfolio of the Leader of the Council)**

**Treasury Management Annual Report & Review of Prudential Indicators 2015/16**

**Purpose of Report**

1. The Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code). Prudential indicators are attached at Annex 1.

2. The regulatory environment places responsibility on members for the review and scrutiny of treasury management policies and activities. This report provides details of the outturn position and highlights compliance with the Council's policies previously approved by members.

**Recommendations**

3. Executive is asked to:

   a. Note the 2015/16 performance of treasury management activity and
   b. Note the compliance with and movements of the prudential indicators in Annex 1

   Reason: to ensure the continued performance of the Council's treasury management function can be monitored.

**Analysis**

**The Economy and Interest Rates**

4. Market expectations for the first increase in Bank Rate moved considerably during 2015/16, starting at quarter 3 2015 but soon moving back to quarter 1 2016. However, by the end of the year, market expectations had moved back radically to quarter 2 2018 due to many fears including concerns that China's economic growth could be heading towards a hard landing, the continuation of the collapse in oil prices during 2015 together with continuing Eurozone growth uncertainties

5. These concerns have caused sharp market volatility in equity prices during the year with corresponding impacts on bond prices and bond yields due to safe haven flows. Bank rate remained unchanged at 0.5% for the seventh successive year. Economic growth in 2015/16 has been disappointing with growth falling steadily from an annual rate of 2.9% in quarter 1 2015 to 2.1% in quarter 4.

6. The sharp volatility in equity markets during the year was reflected in sharp volatility in bond yields. However, the overall dominant trend in bond yields since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have repeatedly been revised downwards and expectations of increases in central rates have been pushed back. In addition, a notable trend in the year was that several central banks introduced negative interest rates as a measure to stimulate the creation of credit and hence economic growth.

7. The UK government maintained its tight fiscal policy stance but the more recent downturn in expectations for economic growth has made it more difficult to return the public sector net borrowing to a balanced annual position within the period of this parliament.

**Overall Treasury Position as at 31 March 2016**

8. The Council's year end treasury debt and investment position for 2015/16 compared to 2014/15 is summarised in the table below:

**Debt**

| **Debt** | **31/03/2016 £m** | **Rate %** | **31/03/2015 £m** | **Rate %** |
|---|---|---|---|---|
| General Fund Debt | 126.7 | 4.20 | 128.8 | 4.18 |
| Housing Revenue | 140.3 | 3.34 | 140.3 | 3.40 |

| | | | | |
|---|---|---|---|---|
| Account Debt | | | | |
| **Total Debt** | **267.1** | 3.75 | **269.1** | 3.74 |
| **Investments** | | | | |
| Councils Investment Balance | 77.2 | 0.56 | 60.997 | 0.52 |

Table 1 summary of year end treasury position as at 31 March 2016

9. The expectation for interest rates within the treasury management strategy for 2015/16 anticipated low but rising Bank Rate, (starting in quarter 1 of 2016) and gradual rises in medium and longer term fixed borrowing rates during 2016/17. Variable, or short term, rates were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

10. In this scenario the treasury strategy was to postpone borrowing to avoid the cost of holding higher levels of investments and to reduce counter party risk.

11. The sharp volatility in equity markets during the year was reflected in sharp volatility in bond yields. However, the overall dominant trend in bond yields since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have been repeatedly revised downwards and expectations of increases in central rates have been pushed back.

**Borrowing Outturn 2015/16**

12. The Councils capital expenditure impacts upon the level of borrowing and the prudential indicators which control the borrowing activity of the Council are contained in Annex 1.

13. The purpose of the Council's underlying need to borrow is to finance capital expenditure, termed the Capital Financing Requirement (CFR). The total CFR for the council at the end of 2015/16 was £319.4m (compared to £ 317.4m 2014/15) split between the General Fund at £179.1m and the HRA at £140.3m.

14. The CFR suggests the Councils level of borrowing could be as high as £319.4m, however in accordance with the flexibility allowed by the borrowing strategy it currently stands at £267.1m. The Council continues make efficient use of its strong cash balance position to support its current capital expenditure requirements and no new borrowing was undertaken during the year.

15. The Council did not restructure any of its borrowing during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

**Investment Outturn 2015/16**

16. All investment activity during the year was carried out in accordance with the approved treasury management strategy and the Council had no liquidity difficulties in meeting its obligations

17. The Council maintained an average investment balance of £104.57m compared to £74.792m in 2014/15. The surplus funds earned an average rate of return of 0.555% in 2015/16 compared to 0.521% in 2014/15. There has been a gradual increase in cash balances over recent years to due the level of developer's contributions held pending investment through the capital programme, along with the continued early receipt of grant funding from Government in advance of spending. These balances are therefore not available in the longer term and will start to decrease as capital investment is made in a range of projects, as outlined in the Capital Strategy approved by Council in February 2016.

18. The comparable performance indicator for the Councils investment performance is the average London Inter Bank Bid Rate that represents average interest rate which major London banks borrow from other banks. Table 2 shows the rates for financial year 2015/16 and shows that for all cash holdings the rate of return exceeds the levels of the usual 7 day and 3 month benchmarks.

| Benchmark | Benchmark Return | Council Performance | CYC Variance |
|---|---|---|---|
| 7 day | 0.36 | 0.55 | +19 |
| 3 month | 0.46 | 0.55 | +9 |

Table 2 – LIBID vs. CYC comparison

## Consultation

19. Not applicable.

## Options

20. Not applicable.

## Corporate Priorities

21. Treasury Management is aimed at ensuring the Council has sufficient liquidity to allow it to operate, safeguards its investments through a prudent investment approach and maximises its return on investments and minimises the cost of its debts. Effective management allows more resources to be freed up to invest in the Council's priorities, values and imperatives, as set out in the Council plan.

## Financial Implications

22. Contained throughout the main body of the report.

## Legal Implications

23. Treasury Management activities have to conform to the Local Government Act 2003, which specifies that the Council is required to adopt the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice.

## Other Implications

24. There are no human resource, equalities, crime and disorder, information technology, property or other implications as a result of this report.

## Risk Management

25. The treasury function is a high-risk area due to the level of large money transactions that take place. As a result of this there are strict procedures set out as part of the Treasury Management Practices statement. The scrutiny of this and other monitoring reports is carried

out by Audit & Governance Committee as part of the council’s system of internal control

### *Contact Details*

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**Annexes**

Annex 1: Prudential Indicators 2015/16