Status of Report:	**Public**	**Agenda Item:**	**13**

Meeting: **Combined Fire Authority**

Date: **24th September 2015**

Subject: **Annual Treasury Management Report 2014/15**

Report By: **The Treasurer**

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For: **Information Only**

1. Purpose

The report presents to the Combined Fire Authority (CFA) the Annual Treasury Management Report 2014/15.

2. Recommendations

The CFA is asked to note the Annual Treasury Management Report for 2014-15.

3. Executive Summary

The Annual Treasury Management Report covers the economy and interest rates; the CFA's treasury position as at 31st March 2015; the strategy for the year; the borrowing requirement and debt; borrowing rates; the borrowing outturn position; investment rates; investment outturn; and performance measurement.

4. Report Detail

4.1. The CFA 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 for 2014/15. This report meets both the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

4.2. During 2014/15 the minimum reporting requirements were that the CFA should receive an annual treasury strategy in advance of the year (CFA 12th February 2014); a mid-year (minimum) treasury update report (CFA 10th December 2014); and an annual review following the end of the year describing the activity compared to the strategy (this report). The regulatory environment places responsibility on Members for the review and scrutiny of treasury management policy and activities. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the CFA's policies previously approved by Members.

4.3. The CFA also confirms that it will comply with the requirement under the Code to give scrutiny to future treasury management reports by the Members of the Corporate

Governance Committee before they are reported to the CFA. Member training on treasury management issues was last undertaken on the 11th December 2013 in order to support Members' scrutiny role.

4.4. The purpose of this report is to meet one of the above requirements of the CIPFA Code, namely the annual review report of treasury management activities.

4.5. The annual review report is to be found at the **Appendix.**

5. Report Implications / Impact

5.1. ***Legal (including crime and disorder)***

None.

5.2. ***Financial (including value for money, benefits and efficiencies)***

These are contained within the main body of this report.

5.3. ***Risk (including corporate and operational, health and safety and any impact on the continuity of service delivery)***

It is important to be aware of risk in respect of treasury management activities, both in investing and borrowing. The CFA has retained Capita as treasury management advisors to ensure that the CFA's treasury activities are appropriate.

5.4. ***Staff, Service Users and Stakeholders (including the Equality Impact Assessment)***

None.

5.5. ***Environmental***

None.

5.6. ***Impact upon Our Plan Objectives***

None.

6. Background Papers

a) Budget 2015-16 (CFA Report - 11th February 2015)

b) Treasury Management mid-year review report 2014-15 (CFA Report - 10th December 2014)

c) Medium Term Financial Plan 2014-17 (CFA Report - 12th February 2014)

7. Appendix

Annual Treasury Management Report 2014

Appendix

Annual Treasury Management Report 2014/15

1. The Economy and Interest Rates

1.1. The original market expectation at the beginning of 2014/15 was for the first increase in Bank Rate to occur in quarter 1 of 2015 as the unemployment rate had fallen much faster than expected through the Bank of England's initial forward guidance target of 7%. In May, however, the Bank revised its forward guidance. A combination of very weak pay rises and inflation above the rate of pay rises meant that consumer disposable income was still being eroded and in August the Bank halved its forecast for pay inflation in 2014 from 2.5% to 1.25%. Expectations for the first increase in Bank Rate therefore started to recede as growth was still heavily dependent on buoyant consumer demand.

1.2. During the second half of 2014 financial markets were caught out by a halving of the oil price and the collapse of the peg between the Swiss franc and the euro. Fears also increased considerably that the European Central Bank (ECB) was going to do too little too late to ward off the threat of deflation and recession in the Eurozone (EZ). In mid-October, financial markets had a major panic for about a week. By the end of 2014, it was clear that inflation in the UK was going to head towards zero in 2015 and possibly even turn negative. In turn, this made it clear that the Monetary Provision Currency (MPC) would have great difficulty in starting to raise Bank Rate in 2015 while inflation was around zero and so market expectations for the first increase receded back to around quarter 3 of 2016.

1.3. Gilt yields were on a falling trend for much of the last eight months of 2014/15 but were then pulled in different directions by increasing fears after the anti-austerity parties won power in Greece in January; developments since then have increased fears that Greece could be heading for an exit from the euro. While the direct effects of this would be manageable by the EU and ECB, it is very hard to quantify quite what the potential knock on effects would be on other countries in the EZ once the so called impossibility of a country leaving the EZ had been disproved.

1.4. Another downward pressure on gilt yields was the announcement in January that the ECB would start a major programme of quantitative easing, purchasing EZ government and other debt in March. On the other hand, strong growth in the US caused an increase in confidence that the US was well on the way to making a full recovery from the financial crash and would be the first country to start increasing its central rate, probably by the end of 2015. The UK would be closely following it due to strong growth over both 2013 and 2014 and good prospects for a continuation into 2015 and beyond. However, there was also an increase in concerns around political risk from the general election due in May 2015.

2. Overall Treasury Position as at 31st March 2015

At the beginning and end of 2014/15 the CFA's treasury position was as follows:

	31st March 2014			31st March 2015		
	Principal	Rate/ Return	Average Life	Principal	Rate/ Return	Average Life
	£m	%	Yrs	£m	%	Yrs
Public Works Loans Board (PWLB) Debt	16.728	3.77	20	15.728	3.84	19
Finance Leases	6.615	3.72	6	5.703	3.67	6
Short-Term Loan	0			1.500	0.65	0
Capital Financing Requirement (CFR)	22.594			23.171		
Over/ (under) borrowing	748			(240)		
Total Investments	5.471	0.58		4.768	0.60	
Net Debt	17.872			18.163		

3. The Strategy for 2014-15

3.1. The expectation for interest rates within the strategy for 2014/15 anticipated low but rising Bank Rate (starting in quarter 1 of 2015), and gradual rises in medium and longer term fixed borrowing rates during 2014/15. 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.

3.2. In this scenario, the treasury strategy was to postpone borrowing to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

3.3. The actual movement in gilt yields meant that PWLB rates saw little overall change during the first four months of the year but there was then a downward trend for the rest of the year with a partial reversal during February.

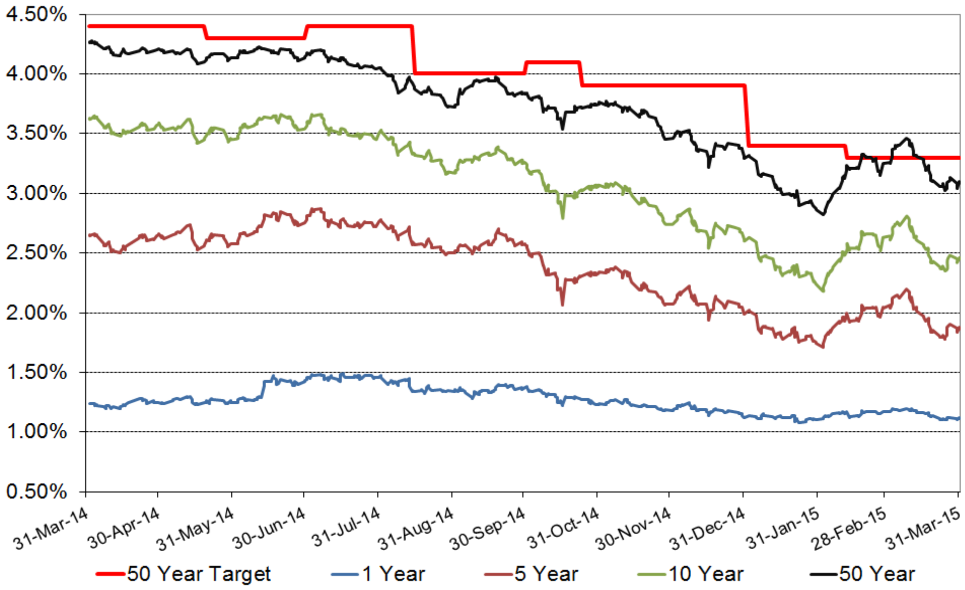
4. The Borrowing Requirement and Debt

The CFA's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR):

	31st March 2014		31st March 2015	
	Budget	Actual	Budget	Actual
	£m	£m	£m	£m
Capital Financing Requirement	28.605	22.594	24.087	23.171

5. Borrowing Rates in 2014/15

PWLB borrowing rates - the graph below shows how PWLB certainty rates have started to rise towards the end of the year after hitting historically low levels.



6. Borrowing Outturn for 2014-15

6.1. Due to investment concerns, both counterparty risk and low investment returns, no long-term borrowing was undertaken in the year. To assist with liquidity the following short-term loans were utilised during the year:

Lender	Principal	Type	Interest Rate	Maturity
	£m		%	
North Yorkshire County Council	1.000	Fixed interest	0.44	Approx. 1 month to 28/07/14
North Yorkshire County Council	1.500	Fixed interest	0.65	Approx. 7 months to 15/07/15

6.2. This compares with a budget assumption of borrowing at an interest rate of 4.65%. The CFA continued to be eligible to access PWLB certainty rate.

6.3. The following long-term loans are outstanding as at 31st March 2015:

Public Works Loans Board Loans				
Date Raised	Rate		Amount £000	Maturity Date
07/08/1997	6.875%		390	30/06/2057
07/08/1997	6.875%		389	30/06/2056
23/07/1998	5.500%		165	30/06/2058
13/10/1998	4.625%		165	30/06/2058

14/01/1999	4.375%		322	31/12/2058
11/08/1999	4.500%		80	30/06/2059
11/08/1999	4.500%		435	30/06/2059
26/06/2000	4.875%		250	30/06/2015
23/11/2000	4.750%		91	30/06/2021
03/07/2001	5.125%		300	30/06/2026
06/09/2001	4.875%		290	30/06/2026
06/12/2005	4.250%		1,635	31/12/2030
27/03/2008	4.550%		460	31/12/2032
01/07/2008	4.890%		756	30/06/2033
20/08/2010	2.020%		1,000	30/06/2015
14/05/2012	3.000%		1,000	31/12/2021
11/12/2012	2.830%		1,000	30/06/2024
11/12/2012	1.800%		500	30/06/2018
15/03/2013	2.820%		1,000	31/12/2022
07/10/2013	3.980%		750	30/06/2028
07/10/2013	2.900%		750	30/06/2020
28/01/2014	3.770%		2,000	30/06/2025
04/03/2014	3.980%		2,000	30/06/2029
Average Rate	**3.835%**	**Total**	**15,728**	

Finance Leases				
Lessor	**Outstanding £000**	**Interest Rate**	**Start Year**	**Expiry Year**
Santander Asset Finance	81	4.96	2005-06	2015-16
SG Equipment Finance	29	4.99	2005-06	2015-16
Lombard North Central	200	5.78	2006-07	2016-17
Clydesdale Asset Finance	303	5.99	2007-08	2017-18
Clydesdale Asset Finance	275	3.74	2009-10	2018-19
Clydesdale Asset Finance	156	4.08	2009-10	2023-24
JCB Finance	422	4.40	2009-10	2018-19
Siemens Financial Services	526	3.58	2009-10	2019-20
JCB Finance	218	4.16	2009-10	2021-22
Santander Asset Finance	722	2.74	2010-11	2020-21
Santander Asset Finance	78	2.74	2010-11	2022-23
Santander Asset Finance	334	2.22	2011-12	2020-21
Santander Asset Finance	210	2.35	2012-13	2020-21
Santander Asset Finance	257	2.10	2012-13	2024-25
SG Equipment Finance	590	2.86	2012-13	2021-22
Siemens Financial Services	1,302	1.86	2013-14	2022-23

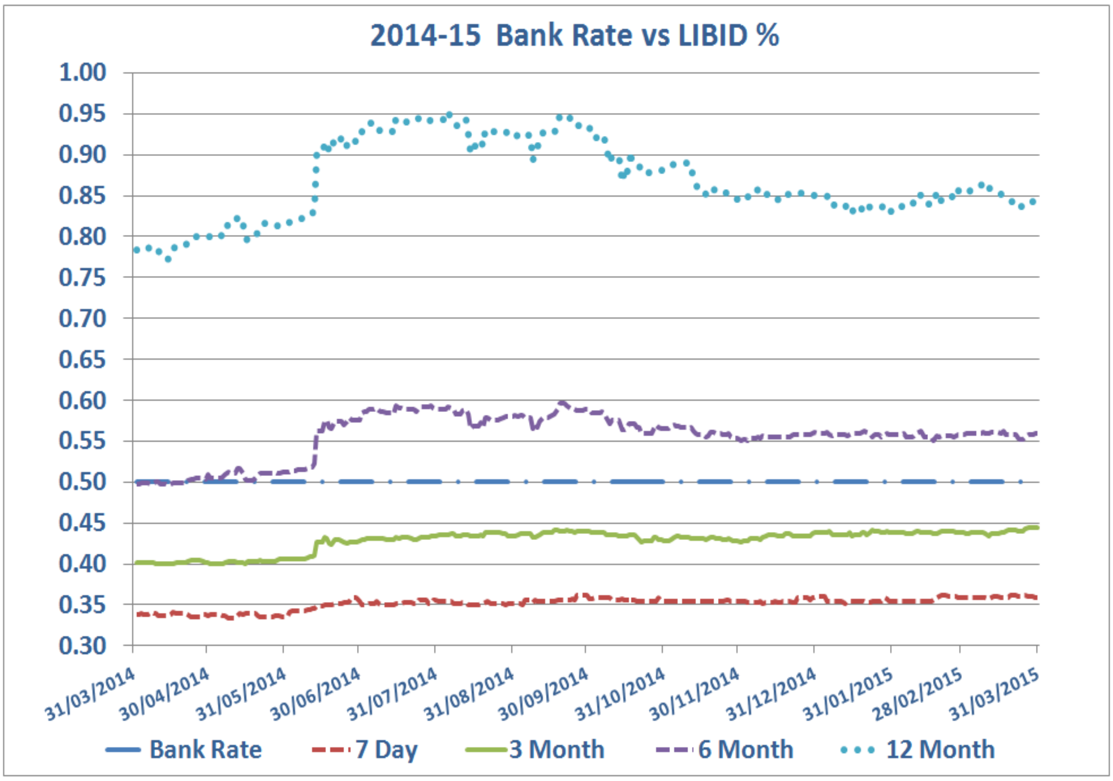
Total	**5,703**			

7. Debt Rescheduling

No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

8. Investment Rates in 2014-15

Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for six years. Market expectations as to the timing of the start of monetary tightening started the year at quarter 1 2015 but then moved back to around quarter 3 2016 by the end of the year. Deposit rates remained depressed during the whole of the year, primarily due to the effects of the Funding for Lending Scheme.



9. Investment Outturn For 2014-15

9.1. Investment Policy:

a) the CFA's investment policy is governed by the Department for Communities and Local Government (DCLG) guidance, which was been implemented in the annual investment strategy approved by the CFA on 12th February 2015. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

b) Due to the continuing limited list of counterparties, and the fact that most require a minimum of £1m as an investment, it has continued to be problematic to maintain percentage balances of less than 50%. In the year to 31st March, 21 days were over 50% with total balances in the £5-£6m range, 28 days were over 50% with total balances in the £6-£7m range, 14 days in the £7-£8m range and 3 days in the £8-£9m range. This will continue to be monitored and reported.

9.2. Investments held by the CFA - the CFA maintained an average balance of £7.780m of internally managed funds. The internally managed funds earned an average rate of return of 0.60%. The comparable performance indicator is the average 7-day LIBID, which was 0.35166%. This compares with a budget assumption of £6.119m investment balances earning an average rate of 1.0%.

10. Prudential and treasury indicators

1. PRUDENTIAL INDICATORS	2013-14	2014-15	2014-15
Extract from budget setting report	**actual**	**original**	**actual**
	£'000	**£'000**	**£'000**
Capital Expenditure	8,316	3,465	3,969
Ratio of financing costs to net revenue stream	5.87%	7.80%	6.67%
Gross borrowing requirement			
brought forward 1 April	13,822	14,432	15,980
carried forward 31 March	15,980	18,384	17,468
in year borrowing requirement	2,158	3,952	1,488
Gross debt	23,343	24,087	22,932
CFR	22,594	24,087	23,171
Annual change in Capital Financing Requirement	2,795	(4,518)	577
Incremental impact of capital investment decisions	**£ p**	**£ p**	**£ p**
Increase in council tax (band D) per annum	7.55	9.64	8.23

2. TREASURY MANAGEMENT INDICATORS	2013-14	2014-15	2014-15
	actual	**original**	**actual**
	£'000	**£'000**	**£'000**
Authorised Limit for external debt -			
borrowing	25,269	21,853	21,853
other long term liabilities	8,336	7,234	7,234
TOTAL	33,605	29,087	29,087
Operational Boundary for external debt -			
borrowing	22,769	19,353	19,353
other long term liabilities	7,836	6,734	6,734
TOTAL	30,605	26,087	26,087
Actual external debt	23,343		22,932
Upper limit for fixed interest rate exposure			

Net principal re fixed rate borrowing / investments	100%	100%	100%
Upper limit for variable rate exposure			
Net principal re variable rate borrowing/ investments	50%	50%	50 %
Upper limit for total principal sums invested for over 364 days			
(per maturity date)	35%	35%	35%

Maturity structure of fixed rate borrowing during 2014/15	upper limit	lower limit
under 12 months	30%	0%
12 months and within 24 months	30%	0%
24 months and within 5 years	30%	0%
5 years and within 10 years	30%	0%
10 years and above	100%	25%