REPORT TO:	Executive Board
DATE:	17 November 2016
REPORTING OFFICER:	Operational Director – Finance
PORTFOLIO:	Resources
TITLE:	Treasury Management Half Year Position 2016-17
WARDS:	Borough-wide

1.0 PURPOSE OF REPORT

1.1 The purpose of this report is to provide an update regarding activities undertaken on the money market as required by the Treasury Management Policy.

2.0 RECOMMENDED: That the report be noted.

3.0 SUPPORTING INFORMATION

Economic Outlook

3.1 The following analysis of the economic situation has been provided by Capita Asset Services, the Council's treasury management advisors.

3.2 During the quarter ended 31st March 2016:

- The UK voted to leave the EU
- Sharp fall in sterling following the referendum result
- The economic recovery lost some momentum ahead of the vote but has remained surprisingly robust since Brexit
- Growth remained highly dependent on consumer spending
- The jobs recovery slowed, but wage growth picked up as household and firms shrugged off referendum uncertainty
- Inflation had remained stuck at very low levels but has started to pick up
- The Bank of England cut interest rates and expanded their asset purchases
- The ECB and the US Fed kept policy unchanged

3.3 UK GDP growth rates in 2013 of 2.2% and 2.9% in 2014 were strong but 2015 was disappointing at 1.8%, though it still remained one of the leading rates among the G7 countries. Growth improved in quarter 4 of 2015 from +0.4% to 0.7% but fell back to +0.4% (2.0% y/y) in quarter 1 of 2016 before bouncing back again to +0.7% (2.1% y/y) in quarter 2. During most of 2015, the economy had faced headwinds for exporters from the appreciation during the year of sterling against the Euro, and weak growth in the EU, China and emerging markets, plus the dampening effect of the Government's continuing austerity programme. The referendum vote for Brexit in June this year delivered an immediate shock fall in confidence indicators and business surveys, pointing to an impending sharp slowdown in the economy. However, subsequent surveys have shown a sharp recovery in confidence and business surveys, though it is generally expected that although the economy will now avoid flat lining, growth will be weak through the second half of 2016 and in 2017.

3.4 The Bank of England meeting on August 4th addressed this expected slowdown in growth by a package of measures including a cut in Bank Rate from 0.50% to 0.25%. The Inflation Report included an unchanged forecast for growth for 2016 of 2.0% but cut the forecast for 2017 from 2.3% to just 0.8%. The Governor of the Bank of England, Mark Carney, had warned that a vote for Brexit would be likely to cause a slowing in growth, particularly from a reduction in business investment, due to the uncertainty of whether the UK would have continuing full access, (i.e. without tariffs), to the EU single market. He also warned that the Bank could not do all the heavy lifting and suggested that the Government will need to help growth by increasing investment expenditure and possibly by using fiscal policy tools (taxation). The new Chancellor Phillip Hammond announced after the referendum result, that the target of achieving a budget surplus in 2020 will be eased in the Autumn Statement on November 23.

3.5 The Inflation Report also included a sharp rise in the forecast for inflation to around 2.4% in 2018 and 2019. CPI has started rising during 2016 as the falls in the price of oil and food twelve months ago fall out of the calculation during the year and, in addition, the post referendum 10% fall in the value of sterling on a trade weighted basis is likely to result in a 3% increase in CPI over a time period of 3-4 years. However, the Monetary Policy Committee is expected to look thorough a one off upward blip from this devaluation of sterling in order to support economic growth, especially if pay increases continue to remain subdued and therefore pose little danger of stoking core inflationary price pressures within the UK economy.

3.6 The American economy had a patchy 2015 with sharp swings in the growth rate leaving the overall growth for the year at 2.4%. Quarter 1 of 2016 disappointed at +0.8% on an annualised basis while quarter 2 improved, but only to a lacklustre +1.4%. However, forward indicators are pointing towards a pickup in growth in the rest of 2016. The Federal Reserve embarked on its long anticipated first increase in rates at its December 2015 meeting. At that point, confidence was high that there would then be four more increases to come in 2016. Since then, more downbeat news on the international scene and then the Brexit vote, have caused a delay in the timing of the second increase which is now strongly expected in December this year.

3.7 In the Eurozone, the European Central Bank commenced in March 2015 its massive €1.1 trillion programme of quantitative easing to buy high credit quality government and other debt of selected Euro Zone countries at a rate of €60bn per month; this was intended to run initially to September 2016 but was extended to March 2017 at its December 2015 meeting. At its December and March meetings it progressively cut its deposit facility rate to reach -0.4% and its main refinancing rate from 0.05% to zero. At its March meeting, it also increased its monthly asset purchases to €80bn. These measures have struggled to make a significant impact in boosting economic growth and in helping inflation to rise from around zero towards the target of 2%. GDP growth rose by 0.6% in quarter 1 2016 (1.7% y/y) but slowed to +0.3% (+1.6% y/y) in quarter 2. This has added to comments from many forecasters that central banks around the world are running out of ammunition to stimulate economic growth and to boost inflation. They stress that national governments will need to do more by way of structural reforms, fiscal measures and direct investment expenditure to support demand in the their economies and economic growth.

3.8 Japan is still bogged down in anaemic growth and making little progress on fundamental reform of the economy while Chinese economic growth has been weakening and medium term risks have been increasing.

Interest Rate Forecast

3.9 The following forecast has been provided by Capita Asset Services.

	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19
Bank rate	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.25%	0.25%	0.25%	0.25%	0.50%
5yr PWLB rate	1.00%	1.00%	1.10%	1.10%	1.10%	1.10%	1.20%	1.20%	1.20%	1.20%	1.30%
10yr PWLB rate	1.50%	1.50%	1.60%	1.60%	1.60%	1.60%	1.70%	1.70%	1.70%	1.70%	1.80%
25yr PWLB rate	2.30%	2.30%	2.40%	2.40%	2.40%	2.40%	2.50%	2.50%	2.50%	2.50%	2.60%
50yr PWLB rate	2.10%	2.10%	2.20%	2.20%	2.20%	2.20%	2.30%	2.30%	2.30%	2.30%	2.40%

Short Term Borrowing Rates

3.10 The bank base rate remained dropped from 0.50% to 0.25% in August 2016

	Mar	Apr	May	Jun	Jul	Aug	Sep
	%	%	%	%	%	%	%
Call Money (Market)	0.48	0.48	0.48	0.48	0.47	0.23	0.22
1 Month (Market)	0.51	0.51	0.52	0.51	0.43	0.27	0.27
3 Month (Market)	0.59	0.59	0.59	0.56	0.49	0.39	0.38

Longer Term Borrowing Rates

	Mar	Apr	May	Jun	Jul	Aug	Sep
	%	%	%	%	%	%	%
1 Year (Market)	1.00	1.02	1.01	0.92	0.80	0.74	0.76
10 Year (PWLB)	2.36	2.51	2.41	1.82	1.69	1.49	1.57
25 Year (PWLB)	3.15	3.22	3.09	2.63	2.47	2.11	2.27

3.11 Market rates are based on LIBOR rates and PWLB rates are for new loans based on principal repayable at maturity. The rates are shown for the end of each month.

Borrowing and Investments

Turnover During the Period

	No of deals	Turnover £m
Short Term Borrowing	2	5
Short Term Investments	17	158

Position at Month End

	Apr £m	May £m	Jun £m	Jul £m	Aug £m	Sep £m
Total Borrowing	165	163	163	163	163	163
Total Investments	(163)	(163)	(163)	(163)	(163)	(153)
Call Account Balance	(20)	(13)	(11)	(14)	(15)	(27)

Investment Benchmarking

Benchmark	Benchmark Return %	Performance Apr - Sep %	Investment Interest Earned £000
7 day	0.28	0.42	36
1 month	0.30	0.00	-
3 month	0.38	0.72	67
6 month	0.52	0.72	308
12 month	0.76	0.76	217
Property Fund		4.30	87
Total			**715**

3.12 This shows the Council has over achieved or matched the benchmark for all maturities for the first 6 months of the year.

3.13 At 30th September 2016 Halton Borough Council holds £5m in the CCLA Local Authority Property Fund. There is no benchmark available for this income.

Budget Monitoring

	Net Interest at 31st March 2016				
	Budget Year to Date £000	**Actual Year to Date £000**	**Variance (o/spend) £000**		**Actual inc M Gateway £000**
Investment	(204)	(438)	234		(715)
Borrowing	571	636	(66)		2,947
Total	**367**	**198**	**169**		**2,232**

3.14 As the borrowing and investments in relation to the Mersey Gateway scheme are to be capitalised they will have no effect on the revenue budget and have therefore been excluded from the budget monitoring figures above.

New Long Term Borrowing

3.15 A £10m loan was taken from the PWLB (Public Works Loan Board) in April 2016. This was to take advantage of historically low 50 year interest rates and is needed to fund the Council's ongoing Capital Programme.

Policy Guidelines

3.16 The Treasury Management Strategy Statement (TMSS) for 2016/17, which includes the Annual Investment Strategy, was approved by the Council on 11 February 2016. It sets out the Council's investment priorities as being:

- Security of capital;
- Liquidity; and
- Yield

3.17 The Council will also aim to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. In the current economic climate and the heightened credit concerns it is considered appropriate to keep the majority of investments short term and to ensure all investments are in in line with Sector's credit rating methodology.

Treasury Management Indicators

3.18 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators were set out in the Treasury Management Strategy Statement and are reviewed in Appendix 1.

3.19 During September 2016 the Council held over 50% of its investments in variable rate instruments, breaking the 30% prudential indicator specified in the Treasury Strategy. This was only a temporary measure due to the payment of the first £35m milestone payment to Merseylink in respect of the Mersey Gateway Project. The Council will be within the 30% limit once this payment is made.

Debt Rescheduling

3.20 No debt rescheduling was undertaken during the quarter.

4.0 POLICY IMPLICATIONS

4.1 None.

5.0 FINANCIAL IMPLICATIONS

5.1 The financial implications are as set out in the report.

6.0 IMPLICATIONS FOR THE COUNCIL'S PRIORITIES

6.1 There are no direct implications, however, the revenue budget and capital programme support the delivery and achievement of all the Council's priorities.

7.0 RISK ANALYSIS

7.1 The main risks with Treasury Management are security of investment and volatility of return. To combat this, the Authority operates within a clearly defined Treasury Management Policy and annual borrowing and investment strategy, which sets out the control framework

8.0 EQUALITY AND DIVERSITY ISSUES

8.1 None.

9.0 LIST OF BACKGROUND PAPERS UNDER SECTION 100D OF THE LOCAL GOVERNMENT ACT 1972

9.1 There are no background papers under the meaning of the Act.

Appendix 1

Treasury and Prudential Indicators – 2016/17 – Quarter 2

	2015/16	2016/17	
Prudential Indicators	**Full Year Actual £000**	**Original Estimate £000**	**Quarter 2 Estimate £000**
Capital Expenditure	29,841	107,715	128,275
Net Financing Need for the Year *(Borrowing Requirement)*	7,094	87,613	100,104
Increase / (Decrease) in CFR *(Capital Financing Requirement)*	3,946	84,417	97,110
Ratio of Financing Costs to Net Revenue Stream *(Proportion of cost of borrowing to Council's net revenue)*	3.2%	2.2%	2.5%
Incremental Impact on band D Council Tax (£) *(net cost of borrowing compared to tax base)*	9.43	2.64	2.42
External Debt	183,000	153,000	163,000
Operational Boundary *(Limit of which external debit is not epected to exceed)*	252,600	255,313	255,313
Authorised Limit *(Limit beyound which external debit is prohibited)*	270,000	270,000	270,000

Upper Limit for Interest Rate Exposure	**Exposure Limit %**	**2015/16 Actual %**	**2016/17 Estimate %**
Fixed Rate	100	100	88
Variable Rate	30	-	12

Maturity Structure of Fixed Rate Borrowing	**Exposure Limit %**	**2015/16 Actual %**	**2016/17 Estiamte %**
Under 12 months	40	7	7
12 months to 24 months	40	7	0
24 months to 5 years	40	0	0
5 years to 10 years	40	0	0
10 years and above	100	86	93

Maximum Principal invested > 365 days	Investment Limit £000	2015/16 Actual £000	2016/17 Estimate £000
Principal Sums Invested over 365 days	30,000	10,000	10,000