OFFICE OF THE POLICE AND CRIME COMMISSIONER
FOR HUMBERSIDE
DECISION RECORD

Decision Record Number: **52/2014**

Title: **Annual Treasury Management Report 2013/14**

Executive Summary:
The Annual Treasury Management Report for 2013/14, which had been recommended by the Audit Committee for approval, was submitted.

Decision:
a) That the Annual Treasury Management Report 2013/14 be approved;
(b) that the total cost of treasury management be identified and opportunities to reduce those costs be sought by seeking opportunities to collaborate with other organisations.

Background Report: Open

Police and Crime Commissioner for Humberside

I confirm I have considered whether or not I have any personal or prejudicial interest in this matter and take the proposed decision in compliance with my code of conduct.

Any such interests are recorded below.

The above decision has my approval.

Signature Matthew Grove **Date 18.12.14**

Humberside Police and Crime Commissioner
Audit Committee
26 September 2014

Agenda Item 6

Report of the Deputy Chief Executive and Treasurer

ANNUAL TREASURY MANAGEMENT REPORT 2013/14

1. The Annual Treasury Management Report provides comprehensive information on treasury management activity undertaken during the period 1 April 2013 – 31 March 2014 and provides a commentary on events affecting the money markets during the financial year.

2. **Recommandations**

   It is recommended that the Committee considers and comments on the Annual Treasury Management Report for 2013/14 prior to submission to the Police and Crime Commissioner for approval.

3. **Background**

   The CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code) underpins the system of capital finance which allows local authorities, including police and crime commissioners (PCCs), to determine their own programmes for capital investment. The Prudential Code has been developed as a professional code of practice to support authorities, PCCs and other organisations, when making decisions on strategic planning, asset management and capital investment.

   The Prudential Code seeks to ensure that there is a clear framework within which to operate so that authorities and PCCs can satisfy themselves that investment plans are considered affordable, prudent and sustainable and that treasury management decisions are taken in accordance with good professional practice. The process is designed to support and record local decision making in a manner that is publicly accountable.

   By Regulation, there is a requirement to have regard to the Prudential Code when carrying out duties in accordance with the Local Government Act 2003. This report demonstrates compliance with the Prudential Code. It also meets the requirements of CIPFA's Code of Practice on Treasury Management.

   A primary requirement of the Code is the formulation and approval by the policy making body, the Police and Crime Commissioner in this case, of a Treasury Management Strategy Statement (TMSS) and details of Treasury Management Practices Statement (TMPS). These set out the responsibilities, delegation and reporting arrangements with regard to treasury management activities.

   The TMSS for 2013/14 and updates to the TMPS were approved by the Commissioner in March 2013. The prudential and treasury indicators were based on the information set out in the Medium Term Financial Strategy (MTFS) which was used to support the precept proposal for 2014/15 which was considered by the Police and Crime Panel (PCP) and subsequently approved by the Commissioner.

   The TMSS requires owners of the policy to receive a minimum of a mid-year review and an annual report on treasury management activities. The mid-year review was submitted to this Committee on 23 December 2013 and was subsequently approved by the Commissioner. Consideration and approval of this report ensures that the requirements of the strategy, and therefore the Code are met.

Treasury Management in this context is defined as: "the management of the organisation's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

The Annual Report has been prepared in conjunction with treasury management advisers Capita Asset Services.

Capita Asset Services provided a detailed briefing on Treasury Management to the Commissioner, Deputy Police and Crime Commissioner and members of this Committee together with senior officers on 6 March 2014.

INFORMATION

The Annual Treasury Management Report for 2013/14 is attached at Annex A.

In addition to this formal report monthly investment reports are produced by Capita Asset Services and posted in the secure area of the website. This can be accessed by members of this Committee.

Officers have access to daily, weekly briefings and news alerts provided by Capita Asset Services and information from a range of other sources including banks, brokers, the media and professional networks.

The report also draws on discussions at Investment Review Meetings chaired by the Deputy Chief Executive and Treasurer and attended by members of the Force's Treasury Management team and other senior finance staff. Meetings were held monthly throughout the year to agree short term actions in light of the latest information on market conditions, creditworthiness of potential counterparties and actual and forecast rates of interest along with details of the current and projected cash flows.

Details of performance and information on the agreed Prudential and Treasury Management Indicators are set out in Appendix 1 to Annex A.

4. **Options**

The reporting requirements are intended to ensure that treasury management activity has been conducted in accordance with the agreed policy and strategy and to demonstrate that operations have been performed within agreed limits. There is no option but to consider this report to ensure compliance with the Prudential Code and to meet reporting requirements.

5. **Risks**

The TMSS sets out detailed information in relation to risks associated with treasury management activity and proposed mitigating actions whilst acknowledging that the risk cannot be entirely eliminated.

The statement, together with the TMPS and the procedures detailed within them are intended to limit the exposure to unforeseen and unbudgeted financial consequences of treasury management activity.

6. **Financial Implications**

The Annual Treasury Management Report sets out details of the treasury management activity undertaken in the period 1 April 2013 to 31 March 2014. The financial implications of this activity have been factored into the budget, budget monitoring reports and medium term financial plans. They reflect in year investment and borrowing assumptions and information on current and predicted cash flows together with actual interest rates and interest rate forecasts.

7. **Legal Implications**

The Police and Crime Commissioner is required to comply with the requirements of the Local Government Act 2003 and to have regard to guidance from the Department for Communities and Local Government and the CIPFA Code when determining its treasury management policy and strategies together with detailed practices.

There is a minimum requirement for a mid-term review of treasury management activity to be considered together with an annual report. The former was considered by this Committee in December 2013 prior to approval by the PCC. This report ensures that the requirements of the strategy, and therefore the Code are met.

8. **Equalities Implications**

There are no equalities implications in the context of the submission.

9. **Consultation**

Capita Asset Services have been consulted on treasury management issues and have provided additional information in relation to the activities undertaken during the year. Officers have also consulted with banks, brokers and have access to treasury management networks to supplement. It must be recognised however that the responsibility for all decisions with regard to policies, strategy and transactions and remains with the PCC and his officers

10. **Media information**

There are not considered to be any particular media issues in relation to this report which is largely technical in nature.

11. **Background documents**

JB File Ref: JB/TM/Annual Report/2013/14

12. **Publication**

The report is open.

Police and Crime Commissioner for Humberside

Annual Treasury Management Report

2013/14

Annual Treasury Management Report 2013/14

1. Introduction

This Police and Crime Commissioner (PCC) is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management report, a review of activities and the actual prudential and treasury indicators for 2013/14. 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).

During 2013/14 the minimum reporting requirements were that the PCC should receive the following reports:

- *an annual treasury strategy in advance of the year (March 2013)*
- *a mid-year (minimum) treasury update report (December 2013)*
- *an annual report following the end of the year describing the activity compared to the strategy (this report)*

The regulatory environment places responsibility for the review and scrutiny of treasury management policy and activities on the PCC. This report is therefore important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the policies previously approved by the PCC. The PCC has established a principle whereby reports are considered and reviewed by the Joint Independent Audit Committee (JIAC) prior to submission to him for approval.

Training on treasury management issues was undertaken during the year in order to support scrutiny of the process. This involved the PCC, the Deputy Police and Crime Commissioner. Members of JIAC and senior officers.

2. The Economy and Interest Rates

The financial year 2013/14 continued the challenging investment environment of previous years, namely low investment returns, although levels of counterparty risk had subsided somewhat. The original expectation for 2013/14 was that Bank Rate would not rise during the year and for it only to start gently rising from quarter 1 2015. Economic growth (GDP) in the UK was virtually flat during 2012/13 but surged strongly during the year. Consequently there was no additional quantitative easing during 2013/14 and Bank Rate ended the year unchanged at 0.5% for the fifth successive year. While CPI inflation had remained stubbornly high and substantially above the 2% target during 2012, by January 2014 it had, at last, fallen below the target rate to 1.9% and then fell further at the end of the financial year. It is also expected to remain slightly below the target rate for most of the two years ahead.

Gilt yields were on a sharply rising trend during 2013 but volatility returned in the first quarter of 2014 as various fears sparked a flight to quality. The Funding for Lending Scheme, announced in July 2012, resulted in a flood of cheap credit being made available to banks which then resulted in money market investment rates falling drastically in the second half of that year and continuing into 2013/14. That part of the Scheme which supported the provision of credit for mortgages was terminated in the first quarter of 2014 as concerns rose over resurging house prices.

The UK coalition Government maintained its tight fiscal policy stance but recent strong economic growth has led to a cumulative, (in the Autumn Statement and the March Budget), reduction in the forecasts for total borrowing, of £97bn over the next five years, culminating in a £5bn surplus in 2018-19.

The EU sovereign debt crisis subsided during the year and confidence in the ability of the Eurozone to remain intact increased substantially. Perceptions of counterparty risk improved after the ECB statement in July 2012 that it would do "whatever it takes" to support struggling Eurozone countries; this led to a return of confidence in its banking system which continued into 2013/14 and led to a move away from only very short term investing. However, this is not to say that the problems of the Eurozone, or its banks, have ended as the zone faces the likelihood of weak growth over the next few years at a time when the total size of government debt for some nations is likely to continue rising and there are concerns over the impact of stress tests on banks within the Eurozone.

3. Overall Treasury Position as at 31 March 2014

At the beginning and the end of 2013/14 the PCC's treasury (excluding finance leases) position was as follows:

TABLE 1	31 March 2013 Principal	Rate/ Return	Average Life yrs	31 March 2014 Principal		Rate/ Return	Average Life yrs
Total debt	***£23.612 m***	***3.85%***	***8.22***	***£30.432 m***		***3.57%***	***7.62***
CFR	***£52.804 m***			***£57.084 m***			
Over / (under) borrowing	***(£29.192 m)***			***(£26.652)m***			
Total investments	***£4.050m***	***0.75%***		***£7.160m***		***0.60%***	
Net debt	***£19.562 m***	***3.10%***		***£23.272 m***		***2.97%***	

4. The Strategy for 2013/14

The expectation for interest rates within the strategy for 2013/14 anticipated low but rising Bank Rate (starting in quarter 1 of 2015), and gradual rises in medium and longer term fixed borrowing rates during 2013/14. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. A cautious approach continued to be *maintained with investment decisions dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.*

In this scenario, the treasury strategy was to postpone borrowing for as long as possible in order to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

The actual movement in gilt yields meant that PWLB rates were on a sharply rising trend during 2013 as markets anticipated the start of tapering of asset purchases by the US Federal Open Market Committee (the Fed). This duly started in December 2013 and the Fed, adopted a future course of monthly reductions of $10bn (from a starting position of $85bn), meaning that asset purchases were likely to stop by the end of 2014. However, volatility set in during the first quarter of 2014 as fears around emerging markets, various vulnerabilities in the Chinese economy, the increasing danger for the Eurozone to drop into a deflationary spiral, and the situation in the Ukraine, caused rates to dip down, reflecting a flight to quality into UK gilts.

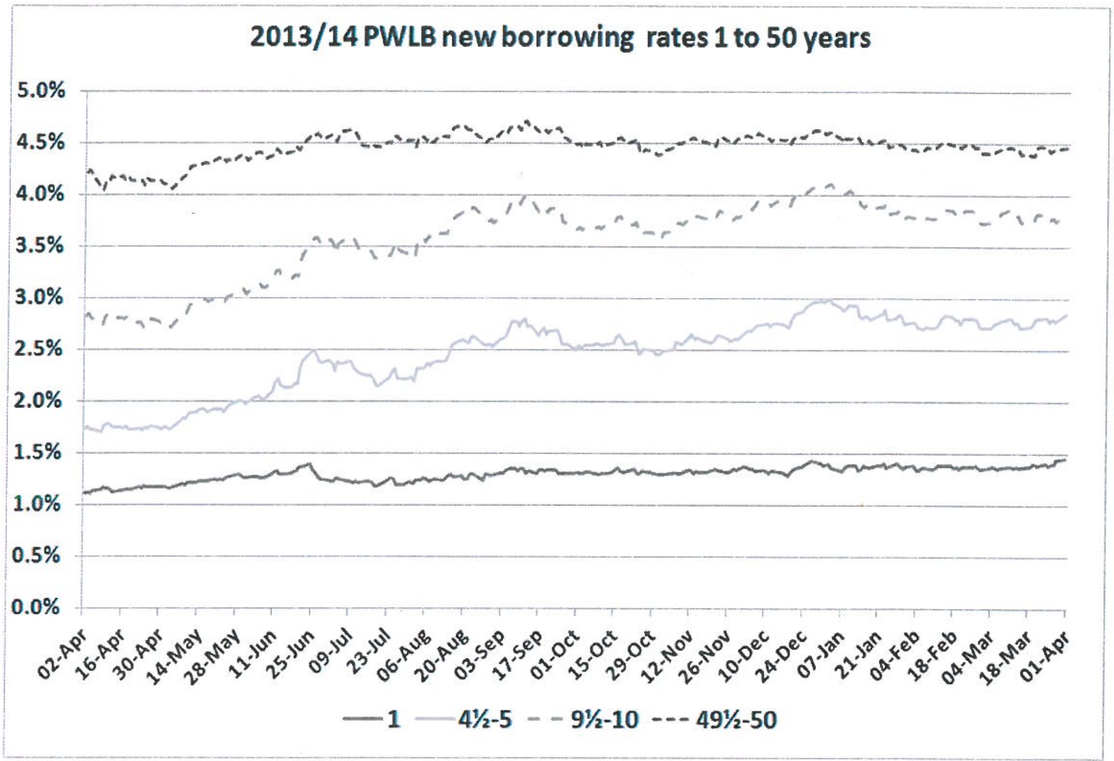
5. The Borrowing Requirement and Debt

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

	31 March 2013 Actual	Original Estimate 2013/14	Revised Estimate 2013/14	31 March 2014 Actual
Total CFR	£52.804m	£71.753m	£59.013m	£57.084m

6. Borrowing Rates in 2013/14

PWLB borrowing rates - the graph below shows how PWLB certainty rates have risen from historically very low levels during the year.



7. Borrowing Outturn for 2013/14

Borrowing – the following loans were taken during the year: -

Lender	Principal	Type	Interest Rate	Maturity
PWLB	£8.0m	Fixed interest rate	2.93%	12 years

This compares with a budget assumption of borrowing at an interest rate of 3.0%.

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

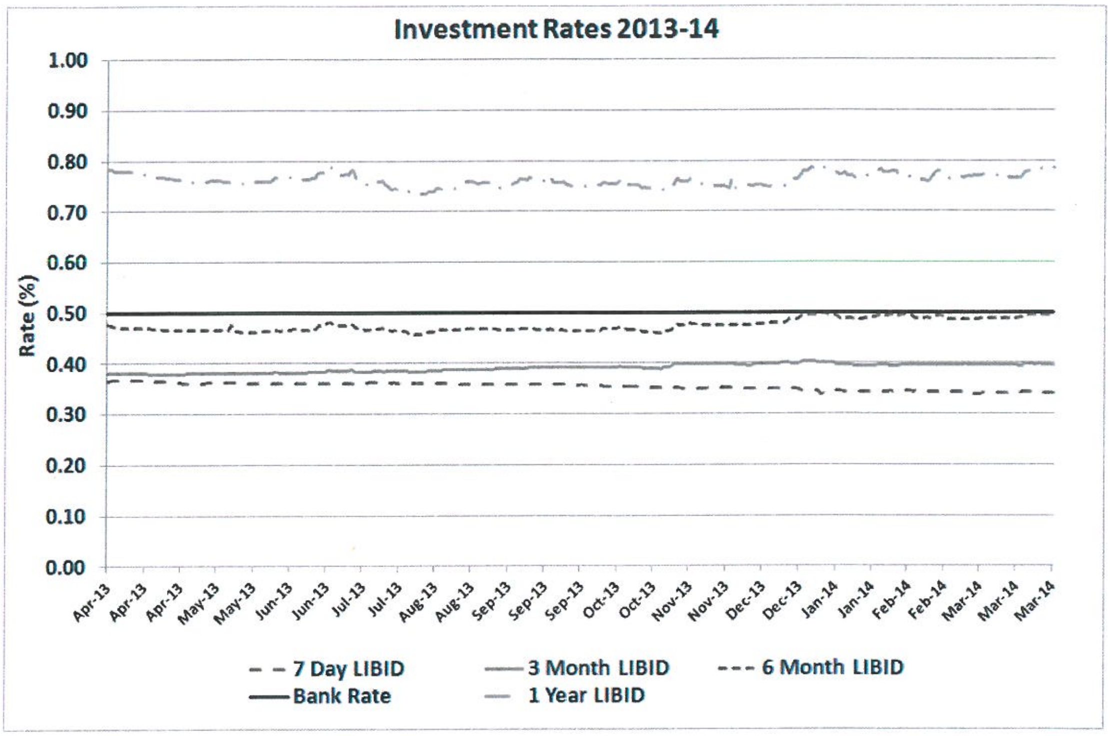
Repayments

The PCC repaid debt in accordance with the terms and conditions of the original loans. No advance re payments of loans were made.

Summary of debt transactions – management of the debt portfolio resulted in a fall in the average interest rate of 0.28%.

8. Investment Rates in 2013/14

Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for five years. Market expectations as to the timing of the start of monetary tightening ended up unchanged at early 2015. The Funding for Lending Scheme resulted in deposit rates remaining depressed during the whole of the year, although the part of the scheme supporting provision of credit for mortgages came to an end in the first quarter of 2014.



9. Investment Outturn for 2013/14

Investment Policy – the PCC's investment policy is governed by CLG guidance, which was been implemented in the annual investment strategy which was incorporated within the TMSS approved in March 2013. This policy set out the approach for choosing investment counterparties, and was 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.).

The investment activity during the year conformed to the approved strategy, and there were no liquidity difficulties during the year.

Investments held by the PCC - the PCC maintained an average balance of £15.374m 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 rate which was 0.36%. This compares with a budget assumption of £5.000m investment balances earning an average rate of 0.80%.

10. Icelandic Bank Defaults

Details of the current position in relation to the investments frozen in Icelandic banks when they failed in 2008 are set out in the PCC and Group financial statements for 2013/14.

The U.K. Government, Local Government Association, administrators and other agencies have continued to work throughout 2013/14 in recovering assets and co-ordinating repayments to all UK councils with Icelandic investments.

The recovery rates are projected to be 94p/£ for the investments in Heritable Bank and 86.5p/£ for Kaupthing Singer and Friedlander. The written down value of these investments at the balance sheet date is now £37k. LAAP bulletins covering the treatment of these investments in the accounts have been issued in previous years but no bulletin was issued in 2013/14 and further guidance is unlikely.

Appendix 1: Prudential and treasury indicators

1. PRUDENTIAL INDICATORS	2012/13	2013/14	2013/14	2013/14
Extract from budget report	Actual	Original Estimate	Revised Estimate	Actual
Capital Expenditure	£14.356m	£17.052m	£9.628m	£7.700m
Ratio of financing costs to net revenue stream	1.07%	1.54%	1.54%	1.44%
Capital Financing Requirement (CFR)	£52.804m	£71.753m	£59.013m	£57.084m
Incremental impact of capital investment decisions	£ p	£ p		£ p
Increase in precept/council tax (band D) per annum	£2.17	£3.62		£2.53

2. TREASURY MANAGEMENT INDICATORS	2012/13	2013/14	2013/14	2013/14
	Actual	Original Estimate	Revised Estimate	Actual
Authorised Limit for external debt -				
borrowing	£85.520m	£88.323m	£73.304m	£73.304m
other long term liabilities	£0.834m	£0.556m	£0.556m	£0.556m
TOTAL	£86.354m	£88.879m	£73.860m	£73.860m
Operational Boundary for external debt -				
borrowing	£83.520m	£86.323m	£71.304m	£71.304m
other long term liabilities	£0.834m	£0.556m	£0.556m	£0.556m

TOTAL	£84.354m	£86.879m	£71.860m	£71.860m
Actual external debt	£23.612m	£30.395m		£30.432m
Upper limit for fixed interest rate exposure	£40.000m	£50.000m		£50.000m
Net principal re fixed rate borrowing / investments	£19.562m			£23.272m
Upper limit for variable rate exposure	£52.500m	£50.000m		£50.000m
Net principal re variable rate borrowing / investments	£0.000m			£0.000m
Principal sums invested for over 364 days*	£0.000m			£0.000m
*All investments are for less than one year				
Maturity structure of fixed rate borrowing during 2013/14	**2012/13 Actual**	**lower limit**	**upper limit**	**2013/14 Actual**
under 12 months	5%	0%	50%	6%
12 months and within 24 months	5%	0%	75%	9%
24 months and within 5 years	24%	0%	80%	26%
5 years and within 10 years	53%	0%	80%	50%
10 years and above	13%	0%	100%	9%