

**OFFICE OF THE POLICE AND CRIME COMMISSIONER  
FOR HUMBERSIDE  
DECISION RECORD**

Decision Record Number: **04/2017**

Title: **Annual Treasury Management Report 2015/16**

**Executive Summary:**

The Annual Treasury Management Report for 2015/16 submitted for approval.

**Decision:**

That the Annual Treasury Management Report 2015/16 be approved.

**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



Date 06.03.2017



**Police and Crime Commissioner for  
Humberside**

**Annual Treasury Management Review  
Report 2015/16**

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# Annual Treasury Management Review Report 2015/16

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## Purpose

This Police and Crime Commissioner (PCC) 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 2015/16. 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 2015/16 the minimum reporting requirements were that the PCC should receive the following reports:

- an annual treasury strategy in advance of the year (approved on 31 March 2015)
- a mid-year treasury update report (approved on 6 January 2016)
- an annual review report following the end of the year describing the activity compared to the strategy (this report)

The regulatory environment places responsibility on the PCC 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 PCC's policies previously approved by members.

This PCC confirms that the requirement under the Code to give prior scrutiny to the strategy and mid-year treasury update reports before they were reported to the PCC was complied with as they were considered at the Joint Independent Audit Committee (JIAC). In the absence of a functioning JIAC, this report has been submitted directly to the PCC. The scrutiny arrangements will recommence when a new JIAC is appointed and becomes operational.

The PCC in office during 2015/16, Senior Officers and JIAC Members involved during the financial year had training on treasury management in order to support them in discharging their respective responsibilities.

## Executive Summary

During 2015/16, the PCC complied with all legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Prudential and treasury indicators	2014/15 Actual £m	2015/16 Original £m	2015/16 Actual £m
Capital expenditure	9.236	10.340	4.627
Capital Financing Requirement	60.849	68.344	59.933
Gross borrowing – External debt	34.986	40.888	31.947
Investments	9.955	2.061	9.650
Net borrowing	25.031	38.827	22.297

*All investments were held for less than one year in line with the PCC's agreed policy.*

Other prudential and treasury indicators are to be found in the main body of this report.

The Deputy Chief Executive and Treasurer also confirms that borrowing has only been undertaken for a capital purpose and the statutory borrowing limit (the authorised limit) was not breached.

The financial year 2015/16 continued the challenging investment environment of previous years, namely low investment returns.

## Introduction and Background

This report summarises the following:-

- Capital activity during the year;
- Impact of this activity on the PCC's underlying indebtedness (the Capital Financing Requirement);
- The actual prudential and treasury indicators;
- Overall treasury position identifying how the PCC has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity.

### 1. Capital Expenditure and Financing 2015/16

The PCC undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the PCC's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

£m	2014/15 Actual	2015/16 Estimate	2015/16 Actual
<b>Capital expenditure</b>	<b>9.236</b>	<b>10.340</b>	<b>4.627</b>
Financed in year	3.220	1.400	2.938
<b>Unfinanced capital expenditure</b>	<b>6.016</b>	<b>8.940</b>	<b>1.689</b>

## 2. Overall Borrowing Need

The PCC's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the PCC's indebtedness. The CFR results from the capital activity of the PCC and resources used to pay for the capital spend. It represents the 2015/16 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the PCC's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury officers organise the PCC's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board [PWLB] or the money markets), or utilising temporary cash resources held by the PCC.

**Reducing the CFR** – the PCC's underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The PCC is required to make an annual revenue charge, called the Minimum Revenue Provision – MRP, to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

The total CFR can also be reduced by:

- the application of additional capital financing resources (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

The PCC's 2015/16 MRP Policy (as required by CLG Guidance) was approved as part of the Treasury Management Strategy Report for 2015/16 in 31 March 2015.

The PCC's CFR for the year is shown below, and represents a key prudential indicator.

CFR (£m): General Fund	31 March 2015 Actual	31 March 2016 Budget	31 March 2016 Actual
Opening balance	57.084	60.849	60.849
Add unfinanced capital expenditure (as above)	6.016	8.940	1.689
Less MRP	( 2.251)	(1.445)	(2.605)
Closing balance	60.849	68.344	59.933

Borrowing activity is constrained by prudential indicators for net borrowing and the CFR, and by the authorised limit.

**Gross borrowing and the CFR** - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the PCC should ensure that gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year 2015/16 plus the estimates of any additional capital financing requirement for the current 2016/17 and next two financial years. This essentially means that the PCC is not borrowing to support revenue



expenditure. This indicator allowed the PCC some flexibility to borrow in advance of immediate capital needs in 2015/16. The table below highlights the PCC's gross borrowing position against the CFR. The PCC has complied with this prudential indicator.

	31 March 2015 Actual	31 March 2016 Budget	31 March 2016 Actual
Gross borrowing position	£34.986m	£40.888m	£31.947m
CFR	£60.849m	£68.344m	£59.933m

**The authorised limit** - the authorised limit is the “affordable borrowing limit” required by s3 of the Local Government Act 2003. Once this has been set, the PCC does not have the power to borrow above this level. The table below demonstrates that during 2015/16 the PCC has maintained gross borrowing within its authorised limit.

**The operational boundary** – the operational boundary is the expected borrowing position of the PCC during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

**Actual financing costs as a proportion of net revenue stream** - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2015/16
Authorised limit	£62.898m
Operational boundary	£60.898m
Average gross borrowing position	£33.467m
Financing costs as a proportion of net revenue stream	2.10%

### 3. Treasury Position as at 31 March 2016

The PCC's debt and investment position is organised by treasury officers in order to ensure adequate liquidity for revenue and capital activities, security of investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through regular reporting and through officer activity detailed in the PCC's Treasury Management Practices Statement. At the end of 2015/16 the PCC's treasury position was as follows:

	31 March 2015 Principal	Rate/ Return	Average Life yrs	31 March 2016 Principal	Rate/ Return	Average Life yrs
Total debt – fixed rate	£34.986m	3.36%	7.25	£31.947m	3.36%	6.46
CFR	£60.849m			£59.933m		
Over / (under) borrowing	£(25.863)m			£(27.986)m		
Total investments	£9.955m	0.59%		£9.650m	0.58%	

The maturity structure of the debt portfolio was as follows:

	31 March 2015 actual	31 March 2016 actual
Under 12 months	£3.038m	£2.740m
12 months and within 24 months	£2.740m	£2.426m
24 months and within 5 years	£9.242m	£10.193m
5 years and within 10 years	£13.735m	£13.803m
10 years and above	£6.231m	£2.785m
<b>Total</b>	<b>£34.986m</b>	<b>£31.947m</b>

The maturity structure of the investment portfolio was as follows:

	31 March 2015 Actual	31 March 2016 Actual
Investments Under 1 year	9.955m	9.650m

*All investments were held for less than one year in line with the PCC's agreed policy.*

The exposure to fixed and variable rates was as follows:

	31 March 2015 Actual	31 March 2016 Actual
Fixed rate (principal or interest) based on net debt	34.986m	31.947m
Variable rate (principal or interest) based on net debt	9.955m	9.650m

## 4. The Strategy for 2015/16

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.

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.

The actual movement in gilt yields meant that the general trend in PWLB rates during 2015/16 was an increase in rates during the first quarter followed by marked bouts of sharp volatility from July 2015 but with an overall dominant trend for rates to fall to historically low levels by the end of the year.

## 5. The Economy and Interest Rates

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 potential destabilisation of some emerging market countries particularly exposed to the Chinese economic slowdown; and the continuation of the collapse in oil prices during 2015 together with continuing Eurozone growth uncertainties.

These concerns 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, therefore, remained unchanged at 0.5% for the seventh successive year. Economic growth (GDP) in the UK surged strongly during both 2013/14 and 2014/15 to make the UK the top performing advanced economy in 2014. However, 2015 was disappointing with growth falling steadily from an annual rate of 2.9% in quarter 1 2015 to 2.1% in quarter 4.

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 materially. These rates continued at very low levels during 2015/16.

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 from July 2015 was for yields to fall to historically low levels as forecasts for inflation were repeatedly been revised downwards and expectations of increases in central rates were 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.

The ECB had announced in January 2015 that it would undertake a full blown quantitative easing programme of purchases of Eurozone government and other bonds starting in March at €60bn per month. This put downward pressure on Eurozone bond yields. There was a further increase in this programme of QE in December 2015. The anti-austerity government in Greece, elected in January 2015 eventually agreed to implement an acceptable programme of cuts to meet EU demands after causing major fears of a breakup of the Eurozone. Nevertheless, concerns that a Greek exit was only being delayed continued.

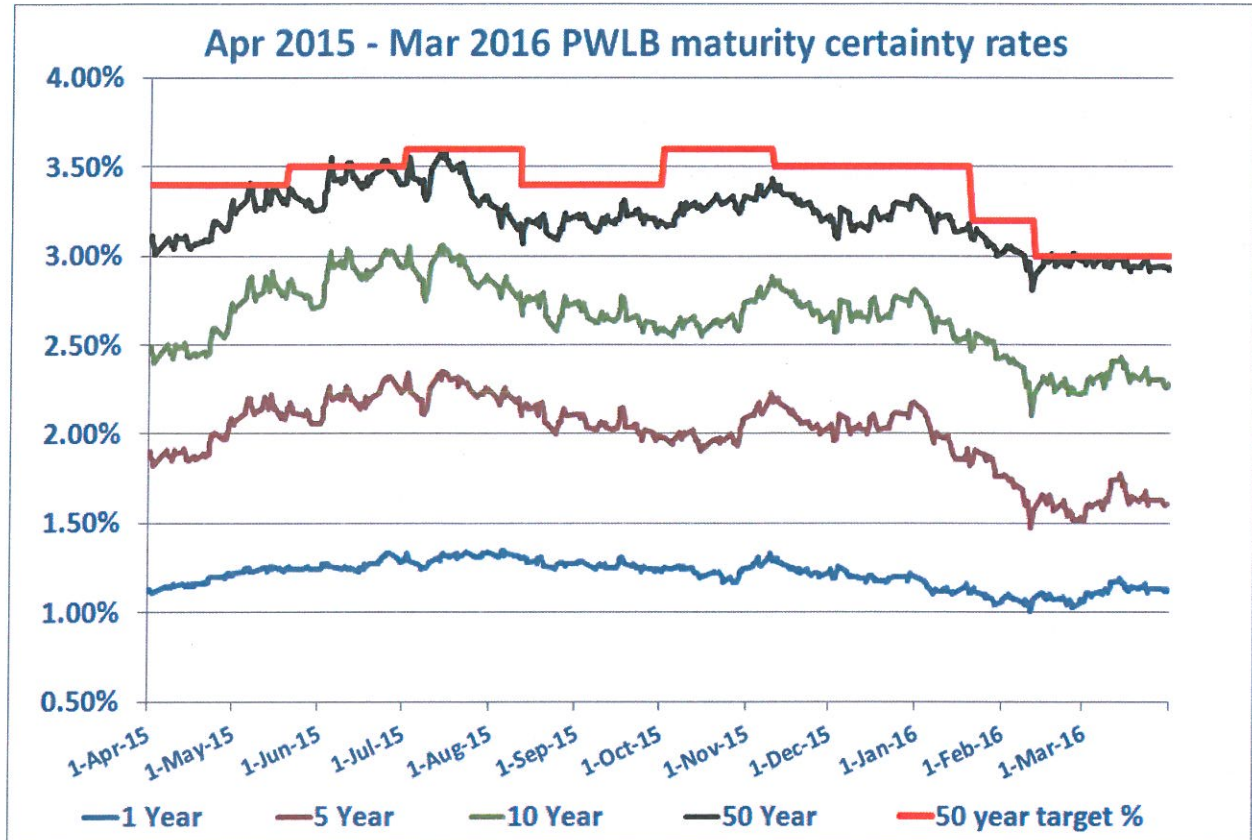
As for America, the economy continued to grow healthily on the back of resilient consumer demand. The first increase in the central rate occurred in December 2015 after which there was caution as to the speed of further increases due to concerns around the risks to world growth.

On the international scene, concerns increased about the slowing of the Chinese economy and also its potential vulnerability to both the bursting of a property bubble and major exposure of its banking system to bad debts. The Japanese economy also suffered disappointing growth in the financial year despite a huge programme of quantitative easing, while two of the major emerging market economies, Russia and Brazil, were in recession. The situations in Ukraine, and in the Middle East with ISIS also contributed to volatility.

The UK elected a majority Conservative Government in May 2015, removing one potential concern but introducing another due to the promise of a referendum on the UK remaining part of the EU. The government maintained its tight fiscal policy stance but a downturn in expectations for economic growth made the prospects of returning public sector net borrowing to a balanced annual position more difficult.

## 6. Borrowing Rates in 2015/16

PWLB **certainty maturity borrowing rates** - the graphs and table for PWLB rates below and in appendix 3, show, for a selection of maturity periods, the average borrowing rates, the high and low points in rates, spreads and individual rates at the start and the end of the financial year.



## Borrowing Outturn for 2015/16

**Treasury Borrowing** – No new borrowing was undertaken during the financial year.

### **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.

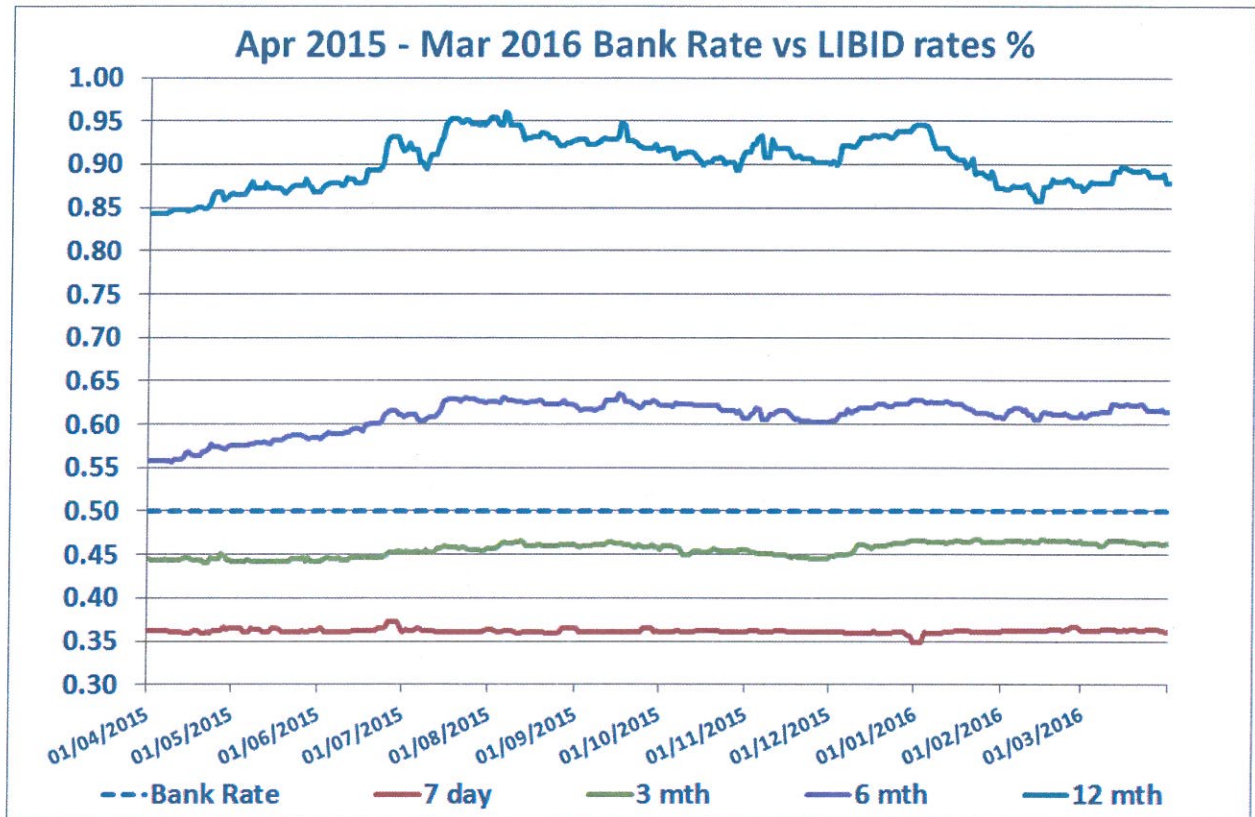
### **Repayments**

The PCC repaid £3.039m at an average rate of 3.04% during the financial year in line with the agreed repayment terms.

**Summary of debt transactions** – management of the debt portfolio resulted in an average interest rate of 3.36%, unchanged from 2014/15.

## 7. Investment Rates in 2015/16

Bank Rate remained at its historic low of 0.5% throughout the year, unchanged for seven years. Market expectations as to the timing of the start of monetary tightening started the year at quarter 1 2016 but then moved back to around quarter 2 2018 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 and due to the continuing weak expectations as to when Bank Rate would start rising.



## 8. Investment Outturn for 2015/16

**Investment Policy** – the PCC’s investment policy is governed by CLG investment guidance, which was implemented in the annual investment strategy approved by the PCC in 31 March 2015. This policy set out the approach for choosing investment counterparties, 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 the PCC had no liquidity difficulties.

**Investments held by the PCC** - the PCC maintained an average balance of £23.392m of internally managed funds. The internally managed funds earned an average rate of return of 0.58%. The comparable performance indicator is the average 7-day LIBID rate, which was 0.36%.



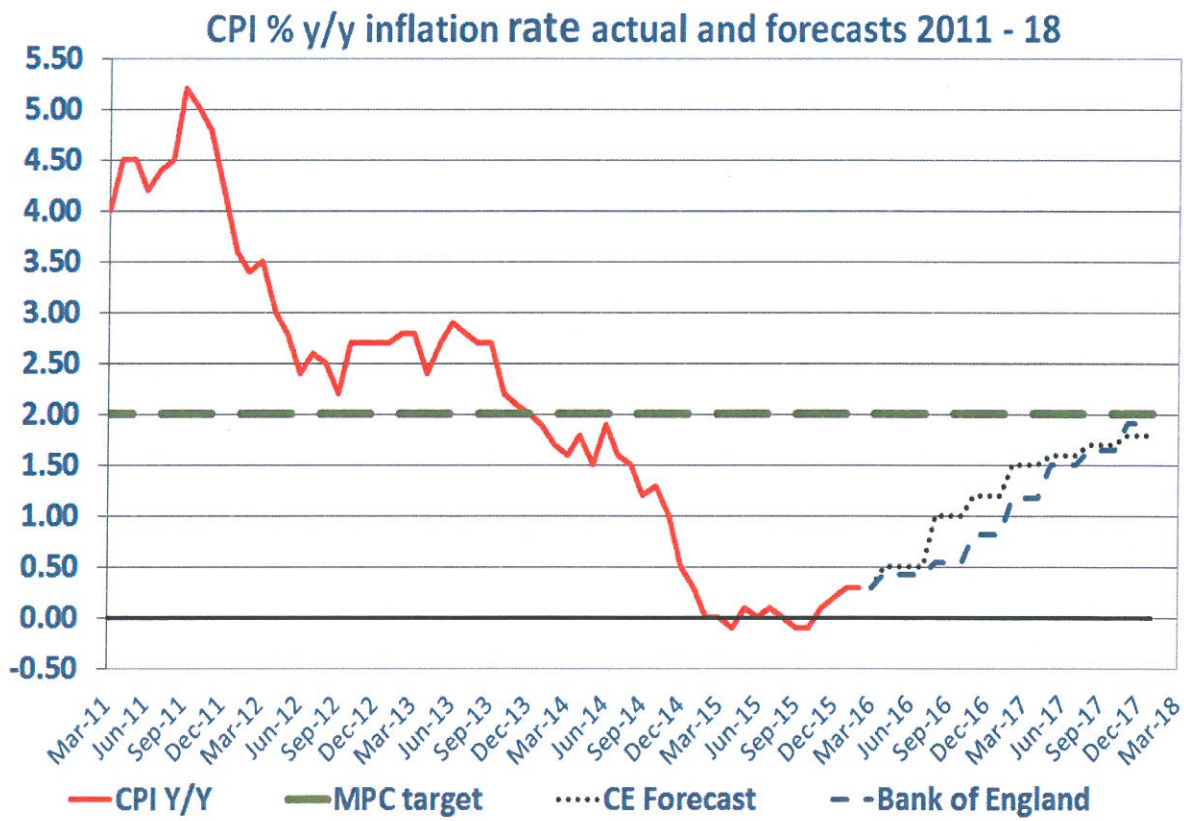
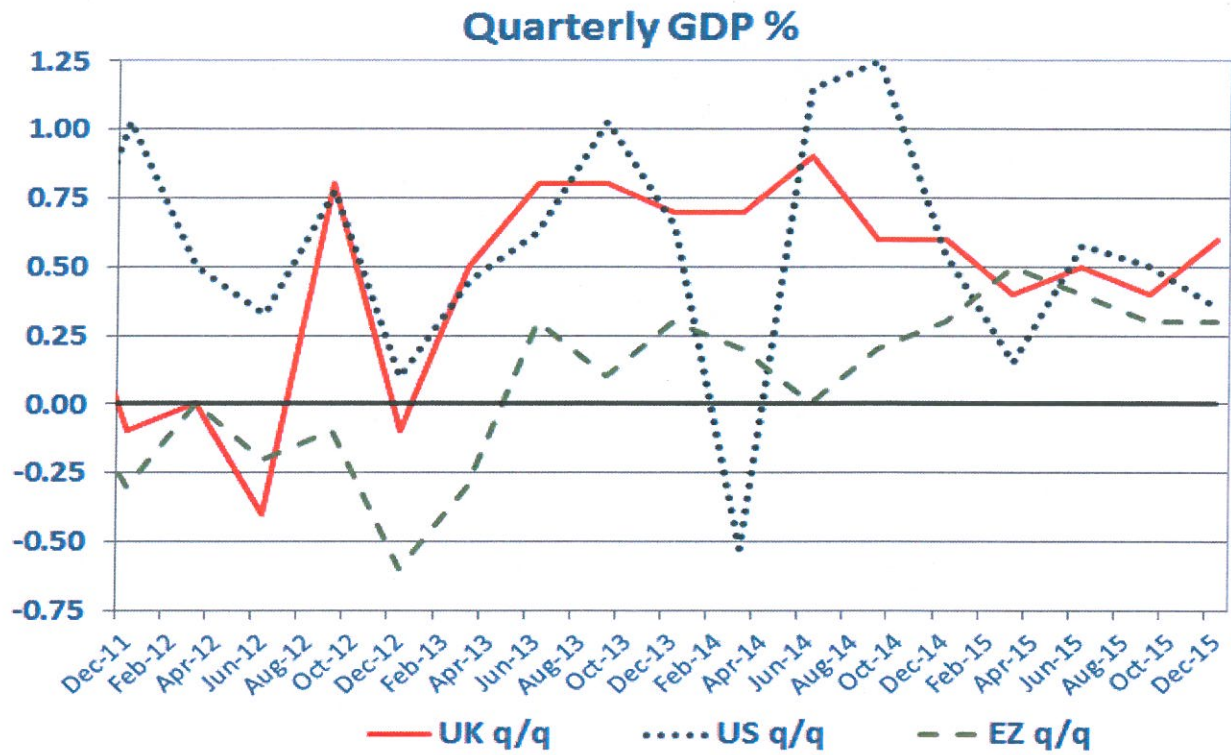
## Appendix 1: Prudential and treasury indicators

1. PRUDENTIAL INDICATORS	2014/15	2015/16	2015/16
	actual	Estimate	actual
Capital Expenditure	£9.236m	£10.340m	£4.627m
Ratio of financing costs to net revenue stream	1.80%	2.65%	2.10%
Gross debt	£34.986m	£40.888m	£31.947m
CFR	£60.849m	£68.344m	£59.933m
Incremental impact of capital investment decisions	£3.64	£5.10	£1.96

<b>2. TREASURY MANAGEMENT INDICATORS</b>	<b>2014/15</b>	<b>2015/16</b>	<b>2015/16</b>
	<b>actual</b>	<b>original</b>	<b>actual</b>
<b>Authorised Limit for external debt -</b>			
borrowing	£59.122m	£68.697m	£62.898m
other long term liabilities	£ 0.294m	£ -	£ -
TOTAL	£59.416m	£68.697m	£62.898m
<b>Operational Boundary for external debt -</b>			
borrowing	£57.122m	£66.697m	£60.898m
other long term liabilities	£ 0.294m	£ -	£ -
TOTAL	£57.416m	£66.697m	£60.898m
<b>Actual external debt</b>	£34.986m	£40.888m	£31.947m
<b>Upper limit for fixed interest rate exposure</b>	£39.756m	£66.000m	£60.000m
<b>Upper limit for variable rate exposure</b>	£1.000m	£32.500m	£29.500m
<b>Upper limit for total principal sums invested for over 364 days*</b>	£0.000m	£0.000m	£0.000m
* All investments are for less than one year			

<b>Maturity structure of fixed rate borrowing during 2015/16</b>	<b>upper limit</b>	<b>lower limit</b>
under 12 months	50%	0%
12 months and within 24 months	75%	0%
24 months and within 5 years	80%	0%
5 years and within 10 years	80%	0%
10 years and above	100%	0%

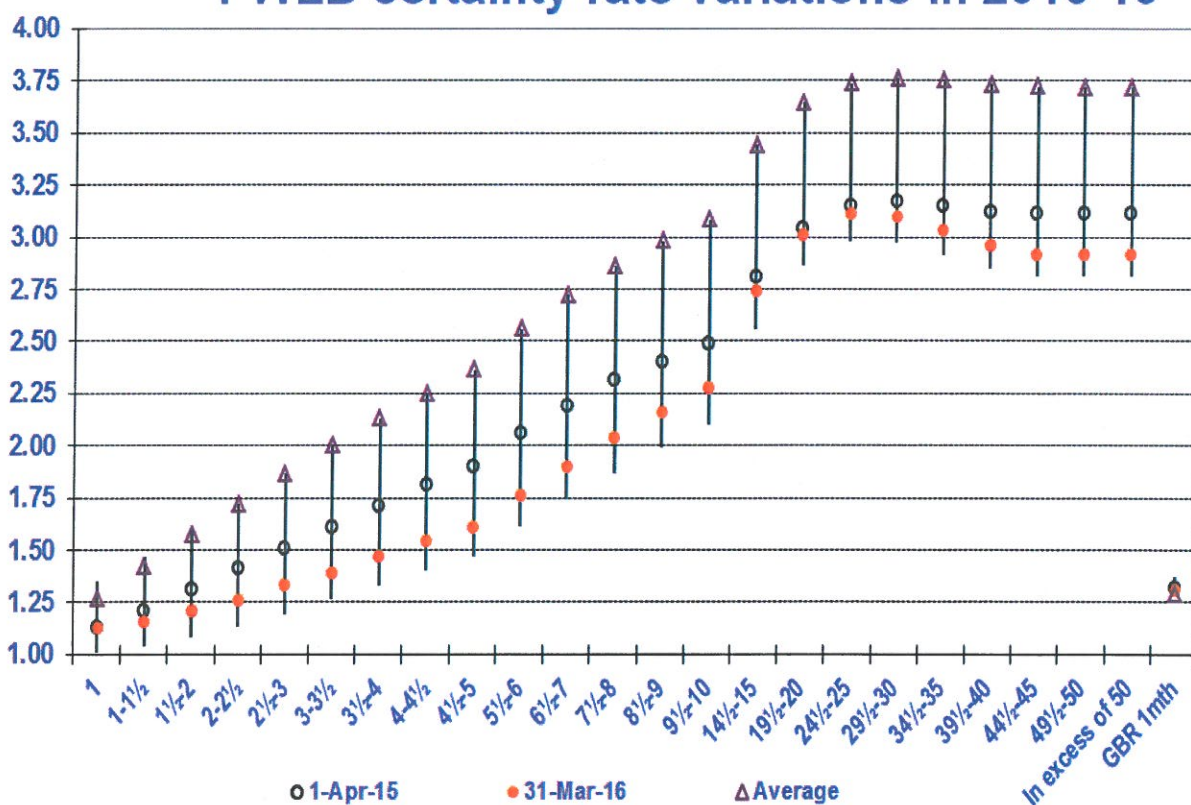
Appendix 2: Graphs



## Appendix 3: Borrowing and investment rates

Money market investment rates 2015/16					
	7 day	1 month	3 month	6 month	1 year
1/4/15	0.361	0.381	0.445	0.559	0.843
31/3/16	0.361	0.386	0.463	0.615	0.878
High	0.372	0.389	0.468	0.635	0.959
Low	0.349	0.377	0.441	0.557	0.842
Average	0.361	0.383	0.456	0.609	0.902
Spread	0.023	0.012	0.027	0.078	0.117
High date	26/6/15	31/11/15	15/2/16	16/9/15	5/8/15
Low date	31/12/15	16/4/15	22/4/15	9/4/15	2/4/15

## PWLB certainty rate variations in 2015-16



	1	1-1.5	2.5-3	3.5-4	4.5-5	9.5-10	24.5-25	49.5-50	1 month variable
1/4/15	1.130%	1.210%	1.510%	1.710%	1.900%	2.490%	3.150%	3.110%	1.320%
31/3/16	1.130%	1.160%	1.330%	1.470%	1.610%	2.280%	3.110%	2.920%	1.310%
High	1.350%	1.470%	1.860%	2.120%	2.350%	3.060%	3.660%	3.580%	1.370%
Low	1.010%	1.040%	1.190%	1.330%	1.470%	2.100%	2.980%	2.810%	1.310%
Average	1.212%	1.302%	1.608%	1.814%	2.004%	2.653%	3.348%	3.216%	1.336%
Spread	0.340%	0.430%	0.670%	0.790%	0.880%	0.960%	0.680%	0.770%	0.060%
High date	05/08/2015	06/08/2015	02/07/2015	15/07/2015	14/07/2015	14/07/2015	02/07/2015	14/07/2015	30/10/2015
Low date	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016	21/03/2016

	1 Year	5 Year	10 Year	25 Year	50 Year
1/4/15	1.13%	1.90%	2.49%	3.15%	3.11%
31/3/16	1.13%	1.61%	2.28%	3.11%	2.92%
Low	1.01%	1.47%	2.10%	2.98%	2.81%
Date	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016
High	1.35%	2.35%	3.06%	3.66%	3.58%
Date	05/08/2015	14/07/2015	14/07/2015	02/07/2015	14/07/2015
Average	1.21%	2.00%	2.65%	3.35%	3.22%

