# REPORTS FROM THE EXECUTIVE AND COMMITTEES TO COUNCIL

## REPORT OF THE REVIEW COMMITTEE

### 1 TREASURY MANAGEMENT ANNUAL REVIEW 2016/17

1.1 This item of business was referred by the Review Committee on 4 July 2017 to Full Council with recommendations on the Council's Treasury Management Annual Review 2016/17. An extract of the key elements of the report of the Section 151 Officer to the Review Committee is at Appendix A.

1.2 In response to questions it was noted that:

1.3 The procurement process for the Treasury Management (TM) advice contract would commence in September 2017; a list of possible organisations to be invited to submit tenders would be drawn up then. It was hoped to bring in as much competition as possible to the tender process although at present there are only two organisations, Capita Asset Services and Arlingclose, which provide a full TM service. Capita is in the process of being bought out but any company taking over will continue to provide the service currently provided by Capita.

1.4 In terms of Member oversight of the tender process, the Treasury Management Strategy Statement is part of the budget process, which would commence in September/October 2017. In addition, a mid-year review will be undertaken by the Review Committee at its meeting on 5 December 2017. It was agreed that the Treasury Management Advisers Review Group would meet in November to review the proposed contract specification and report into the December meeting of the Review Committee.

1.5 The TM service could not be shared with another Authority as the service is tailored to the Council's specific requirements. The Council would procure the basic TM package, as currently offered by Capita, which is appropriate for an authority of Rochford's size. Additional services could be purchased as and when needed.

1.6 The Council had agreed that the TM strategy for 2016 would be to mitigate risk and thus continued to invest in safe funds. The Section 151 Officer had provided the Committee with options for investing in higher risk/higher return investments, including property funds, which could potentially yield 3-4%, but the Council had decided to remain with lower risk investments. The Council was currently looking at investing in a fixed rate investment fund that would yield 0.7%.

1.7 The likelihood of movement in interest rates would be one of the areas to be considered during the 2018/19 budget process. Each month the Capita interest rate sub group meets to discuss interest rates. In the longer term there may be an increase in the base rate, although this may not have any impact on rates for deposits.

1.8 There was a Member request that information be provided on how the investments of those authorities that had invested in higher risk products had performed, so that it could be shown how much this Council could have earned over a specific period had it invested in higher risk products. The officer would ask other authorities if they would be willing to share this information.

1.9 The £6,000 per annum fee paid to Capita was considered to represent value for money. The option of using banks to provide the TM service would be explored by the Principal Finance Officer as part of the procurement process; an update would be provided to the Treasury Management Task and Finish Group at their meeting in November. VAT was payable on this amount but claimed back by the Council.

1.10 The Council's Treasury Management practices will be reviewed in December 2017 as part of the TM Strategy Statement. This would be available for consideration by the Treasury Management Task and Finish Group in November and the Review Committee in December.

## 2 RECOMMENDATION

2.1 It is proposed that Council **RESOLVES**

(1) That the contents of the Treasury Management Annual Review be noted.

(2) That Rochford District Council completes a re-procurement of the Treasury Management and Investment Management services when the contract with Capita Asset Services expires. (S151O)

If you would like this report in large print, Braille or another language please contact 01702 318111.

# TREASURY MANAGEMENT ANNUAL REVIEW 2016/17

## 1 SUMMARY

1.1 This report sets out a summary of the Council's Treasury Management activity for the year 1 April 2016 to 31 March 2017 (2016/17). The report seeks the views of the Review Committee on the information presented in this report before it is submitted for approval by Full Council on 18 July 2017.

1.2 The two major landmark events that had a significant influence on financial markets in the 2016-17 financial year were the UK EU referendum on 23 June 2016 and the election of President Trump in the USA on 9 November 2016. The first event had an immediate impact in terms of market expectations on when the first increase in Bank Rate would happen, pushing it back from quarter 3 2018 to quarter 4 2019.

1.3 At its 4 August 2016 meeting the Monetary Policy Committee (MPC) cut the Bank Rate from 0.5% to 0.25% and the Bank of England's Inflation Report produced forecasts warning of a major shock to economic activity in the UK, which would cause economic growth to fall almost to zero in the second half of 2016. The MPC also warned that it would be considering cutting the Bank Rate again towards the end of 2016 in order to support growth. In addition, it restarted quantitative easing with purchases of £60bn of gilts and £10bn of corporate bonds, and also introduced the Term Funding Scheme whereby potentially £100bn of cheap financing was made available to banks.

1.4 In the second half of 2016, the UK economy confounded the Bank's pessimistic forecasts of August. After a disappointing quarter 1 of only +0.2% GDP growth, the three subsequent quarters of 2016 came in at +0.6%, +0.5% and +0.7% to produce an annual growth for 2016 overall, compared to 2015, of no less than 1.8%, which was very nearly the fastest rate of growth of any of the G7 countries. Needless to say, this meant that the MPC did not cut the Bank Rate again after August but, since then, inflation has risen rapidly due to the effects of the sharp devaluation of sterling after the referendum.

1.5 The Council's income from investment was up against the £30,000 revised budget set for 2016/17, with actual income from treasury management activities being £35,985.

## 2 INTRODUCTION AND BACKGROUND

2.1 Treasury Management is defined as "The management of the local authority's investments, 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".

2.2 For 2016/17 the primary requirements of the CIPFA code, together with how the Council complies, are as follows:-

- Creation and maintenance of a Treasury Management Policy Statement that sets out the policies and objectives of the Council's treasury management activities: this is contained within the Financial Regulations of the Council's Constitution. The Financial Regulations are reviewed annually.
- Creation and maintenance of Treasury Management Practices, which set out the manner in which the Council will seek to achieve those policies and objectives. The Practices were last reviewed and updated in December 2015.
- The Council should receive an Annual Treasury Management Strategy Report (including the Annual Investment Strategy Report) for the year ahead and an Annual Review Report of the previous year. The Strategy for 2016/17 was agreed by Council in February 2016 and this report is the Annual Review Report.
- A mid year treasury report is required detailing the position to date, and any changes in practices. This was reported to the Review Committee in November 2016, and noted by Full Council in December 2016.

All Executive decisions on borrowing, investment or financing are delegated to the Section 151 Officer, as the Chief Finance Officer, and this delegation is documented in the Financial Regulations.

**3 TREASURY MANAGEMENT ADVISORS**

3.1 The Council's contract with Capita Asset Services, for Treasury Management advice, is due to end in February 2018. A project team from the Review Committee met on 26 April 2017 to conduct a review of the contract. It was decided that the Principal Finance Officer would report back to the Review Committee on the following:-

- Other options for providing Treasury Management Services including, but not exclusively, interest rate forecasts, Credit Ratings of Banks and Institutions, together with training for both Members and Officers.
- Whether, with the S151 Officer role currently being procured via Essex County Council (ECC), ECC could provide the advice required through the S151 contract.
- Whether any actions were required of this Authority in terms of ending the S151 Officer role arrangement in February 2018.

3.2 Each point above will now be answered in turn:

3.3 Point 1: In terms of other Treasury Management Advisors, when this Authority went to tender for the contract in 2013, a number of companies were invited to quote. At the time Capita (known as Sector in 2013) was appointed based on price and service provision.

There is a limited market open to Local Authorities for this type of Treasury Management and Investment Management advice. An option could be to split the advice into constituent parts, potentially attracting more providers for the Investment Management element. However, in terms of value for money, as this is a small area of spend overall, it is felt that the set up costs and management overheads from any bidder would outstrip potential savings achieved from more companies vying for the business.

There is also the option of soft market testing which could be carried out over the next three months. The question is whether the Council could engender enough interest in the market place with its typically low capital amounts (less than £10m).

3.4 Point 2: With regard to ECC covering the Treasury Management advice from the existing Section 151 contract, this would not be covered per se. Any advice from ECC would be a combination of advice from the ECC's own advisors combined with the insight from the Chief Accountant. Whilst the Chief Accountant advice is covered within the agreement to a point, the external providers to ECC may insist on either an additional charge to ECC or that ECC does not pass on such advice/insight to third parties. The Chief Accountant advice alone would not be sufficient for RDC's needs.

3.5 Point 3: The Section 151 role, subject to earlier termination in accordance with clause 4.4 of the MOU (quoted below), remains in effect for a minimum period of three years to 6 September 2018. From 1 April 2018 a new MoU may come into effect, with the agreement of both parties.

Clause 4.4 of the MOU: Either organisation may give a minimum of three months written notice to withdraw from this MoU. If such notice is given, each organisation concerned will be responsible for their own costs associated with their withdrawal from this MoU. Each organisation shall take all reasonable steps to mitigate any such costs for the other organisation.

Once ECC ceases to be the provider of the Section 151 role, RDC must have an appropriately qualified person/provider in place to continue as the designated Section 151 officer.

3.6 The Review Committee Project Team also questioned whether any actions were required of this Authority in terms of ending the Capita Assets Services contract arrangement in February 2018.

3.7 The answer to this question is that the Council would have to give one month's notice of its intention either to not renew the contract or of its intention to go out to tender for the service in February 2018. It would be expected that Capita Assets Services would retender for the business if this happened.

## 4 INVESTMENT POSITION

3.1 The investment position at the beginning and the end of the year, as shown on the Council's Balance Sheet, was as follows:-

Balance as at 31 March 2016 £0

Balance as at 31 March 2017 £5.00m

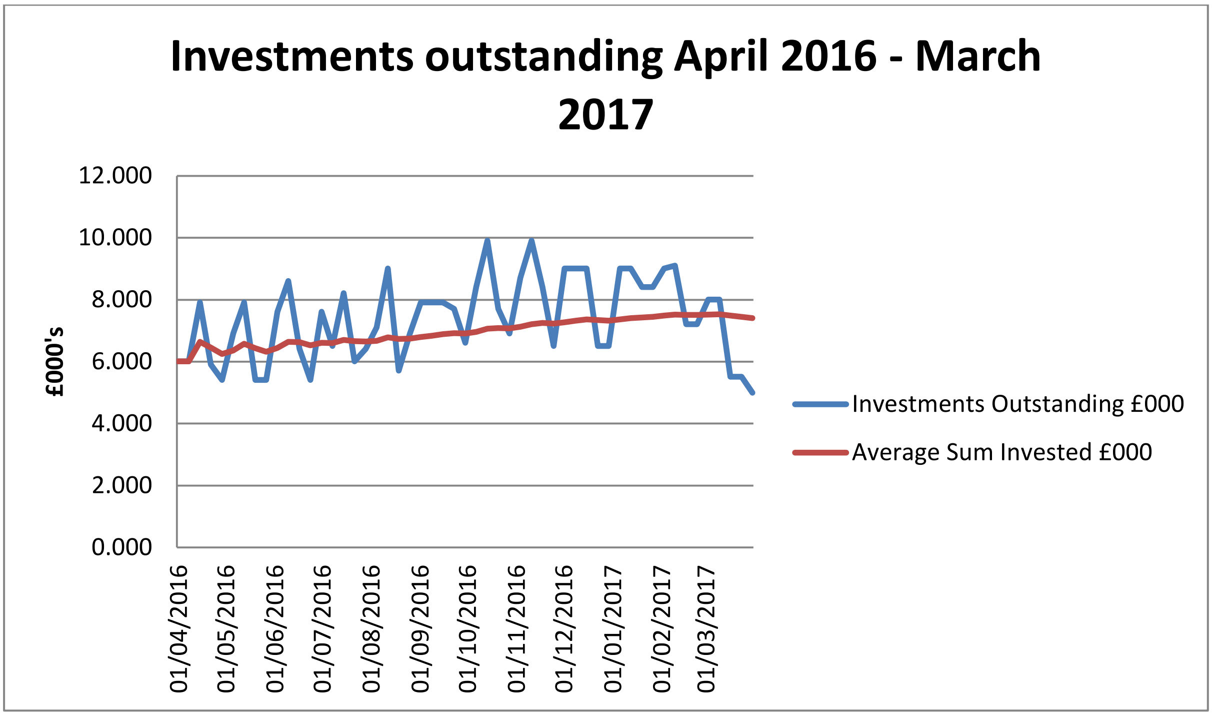
The Authority had no fixed rate investments placed as at 31 March 2017. All investments were in instant access reserve accounts, treated as cash and cash equivalents on the Council's Balance Sheet.

## 5 INVESTMENT PERFORMANCE FOR 2016/17

5.1 The Investment Strategy for 2016/17 was based on expectations that the bank rate would remain at 0.50% during the year. This did not materialise and the base rate was cut to 0.25%. Current forecasts are for the bank rate to remain at 0.25% until June 2019 when a rise to 0.50% is forecast.

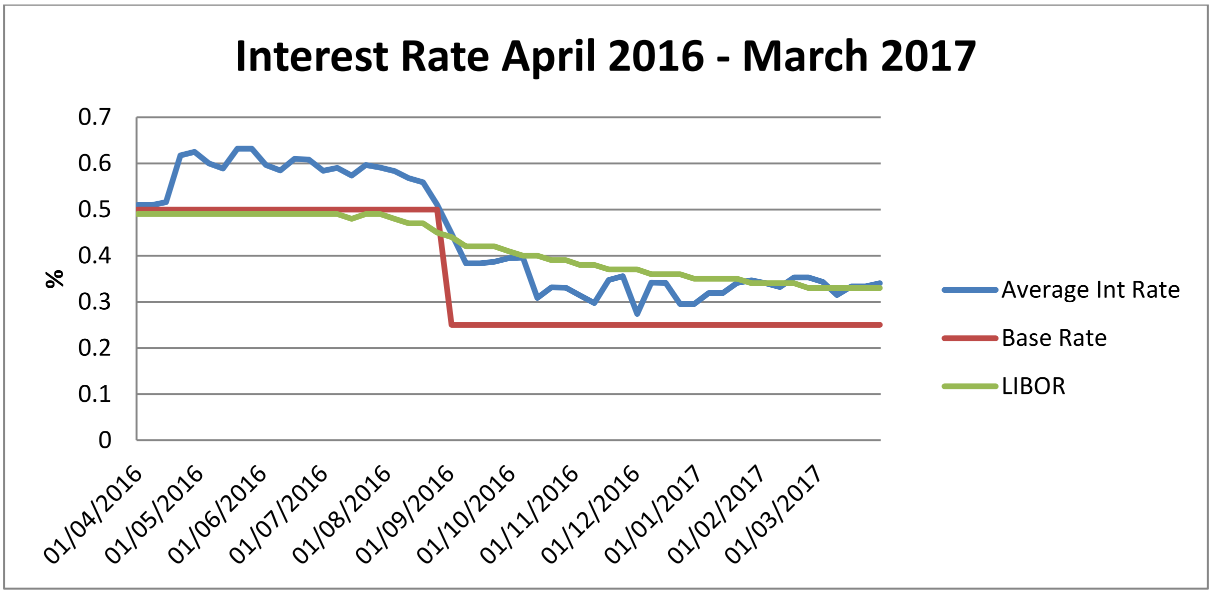
5.2 The majority of investments have been made for cash flow requirements but, where the market has given slightly higher rates in anticipation at the time of future rate increases, the opportunity was also taken to benefit from these.

The graph below shows an increase in average balances from £6.01m to £7.40m at the end of the year.




5.3 Total external interest earned was £35,975, compared to £34,537 in 2015/16. The revised estimate for 2016/17 was £30,000, representing a 19% over achievement.

5.4 The following graph shows a comparison of average rate of interest earned, Bank base rate and the benchmark (7-day London Interbank Rate):-




The graph clearly shows the correlation in average interest rate achieved when compared to The Bank of England Base rate.

5.5 The Authority uses a combination of credit ratings, credit default swaps and market intelligence to decide which banks and financial institutions it will deposit funds with. During 2016/17 there were a number of credit rating changes, resulting in the amount RDC could deposit with any one counterparty changing quite regularly. These changes were actioned as notification was received.

**6 COMPLIANCE WITH TREASURY LIMITS**

During the financial year the Council operated within the Treasury Limits and Prudential Indicators set out in its annual Treasury Strategy Statement. The outturn for the Prudential Indicators, compared to the estimates made in January 2016, are shown below

| PRUDENTIAL INDICATOR | 2014/15 | 2015/16 | 2015/16 |
|---|---|---|---|
| | Actual | Estimate | Actual outturn |
| | | | |
| Capital Expenditure £000s | 1,262 | 3,958 | 3,048 |
| Ratio of Financing Costs to Net Revenue Stream | (0.25%) | (0.37%) | (0.34%) |
| Capital Financing Requirement as at 31 March £000s | 687 | 687 | 687 |
| Incremental Impact of Capital Investment Decisions - (Reduction) in Council Tax (band D) per annum £ | (0.21) | 0.43 | (0.14) |

**7 RESOURCE IMPLICATIONS**

7.1 Investment income used to be an important source of income to the General Fund but that is no longer the case and is unlikely to recover in the medium term. The Capita contract costs £6,000 per year. The advice service frees up officer time from researching the money markets and means that investment decisions are made in a timely fashion.

7.2 All interest received is accounted for within the General Fund. The Authority had no borrowings during the year, so no interest was paid out.

**8 RISK IMPLICATIONS**

8.1 The Treasury Management Strategy discusses in detail the risks involved in making investments and in particular the risk that a building society or bank may fail during the duration of an investment. The Authority is responsible for managing the investment of public funds and must be seen to be adopting a prudent approach. No institutions in which investments were made during

2016/17 had any difficulty in repaying investments and interest in full during the year.