**MUNICIPAL YEAR 2014/2015 REPORT NO. 18**

**MEETING TITLE AND DATE:**
**Cabinet 23rd July 2013**

**REPORT OF:**
Director of Finance, Resources & Customer Services

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| **Agenda – Part: 1** | **Item: 9** |
|---|---|
| **Subject:** **ANNUAL TREASURY MANAGEMENT OUTTURN REPORT 2013/14** **Wards: All** | |
| **Cabinet Member consulted: Cllr. A. Stafford** | |

## 1. EXECUTIVE SUMMARY

1.1 This report reviews the activities of the Council's Treasury Management function over the financial year ended 31 March 2014.

1.2 The key points of the report are highlighted below:

| | | ***See section:*** |
|---|---|---|
| | | |
| **Debt Outstanding at year end to finance capital** | • *£298m an increase of £4.4m from 2012/13.* | ***6*** |
| **Average interest on total debt outstanding** | • 4.53% a reduction of 0.03% from 2012/13. | **7** |
| **Debt Re-scheduling** | • *None undertaken.* | **9** |
| **Interest earned on investments** | • £541k an increase of £215k from 2012/13. | **11** |
| **Net Borrowing** | • *Reduced by £18.5m to £235.3m* | **11** |

## 2. RECOMMENDATIONS

2.1 Cabinet is recommended to accept the Treasury Outturn report.

## 3. BACKGROUND

3.1 The Council adopted the CIPFA Revised Treasury Management Code of Practice and approved the annual Treasury Management Policy Statement in February 2010.

3.2 The statement requires the Director of Finance Resources & Customer Services to report on the preceding year's treasury management activities. In accordance with best practice, the Director's report includes information about borrowing levels and costs, as well as the impact of the cash flow management arrangements on the Council's financial position.

## 4. NATIONAL CONTEXT

4.1 At the beginning of the 2013-14 financial year markets were concerned about lacklustre growth in the Eurozone, the UK and Japan. Lack of growth in the UK economy, the threat of a 'triple-dip' alongside falling real wages (i.e. after inflation) and the paucity of business investment were a concern for the Bank of England's Monetary Policy Committee. Only two major economies – the US and Germany – had growth above pre financial crisis levels, albeit these were still below trend. The Eurozone had navigated through a turbulent period for its disparate sovereigns and the likelihood of a near-term disorderly collapse had significantly diminished. The US government had just managed to avoid the fiscal cliff and a technical default in early 2013, only for the problem to re-emerge later in the year.

4.2 With the appointment of Governor Mark Carney, the Bank of England unveiled forward guidance in August pledging to not consider raising interest rates until the ILO unemployment rate fell below the 7% threshold. In the Bank's initial forecast, this level was only expected to be reached in 2016. Although the Bank stressed that this level was a threshold for consideration of rate increase rather an automatic trigger, markets began pricing in a much earlier rise than was warranted and, as a result, gilt yields rose aggressively.

4.3 The recovery in the UK surprised with strong economic activity and growth. Q4 2014 GDP showed year-on-year growth of 2.7%. Much of the improvement was down to the dominant service sector, and an increase in household consumption buoyed by the pick-up in housing transactions which were driven by higher consumer confidence, greater availability of credit and strengthening house prices which were partly boosted by government initiatives such as Help-to-Buy. However, business investment had yet to recover convincingly and the recovery was not accompanied by meaningful productivity growth. Worries of a housing bubble were tempered by evidence that net mortgage lending was up by only around 1% annually.

4.4 Inflation (CPI) fell from 2.8% in March 2013 to 1.7% in February 2014, the lowest rate since October 2009, helped largely by the easing commodity prices and discounting by retailers, reducing the pressure on the Bank to raise rates. Although the fall in unemployment (down from 7.8% in March 2013 to 7.2% in January 2014) was faster than the Bank of England or indeed many analysts had forecast, it hid a stubbornly high level of underemployment. Importantly, average earnings growth remained muted and real wage growth (i.e. after inflation) was negative. In February the Bank stepped back from forward guidance relying on a single indicator – the unemployment rate – to more complex measures which included spare capacity within the economy. The Bank also implied that when official interest rates were raised, the increases would be gradual – this helped underpin the 'low for longer' interest rate outlook despite the momentum in the economy.

4.5 The Office of Budget Responsibility's 2.7% forecast for economic growth in 2014 forecast a quicker fall in public borrowing over the next few years. However, the Chancellor resisted the temptation to spend some of the proceeds of higher economic growth. In his 2013 Autumn Statement and the 2014 Budget, apart from the rise in the personal tax allowance and pension changes, there were no significant giveaways and the coalition's austerity measures remained on track.

4.6 Gilt yields ended the year higher than the start in April. The peak in yields was during autumn 2013. The biggest increase was in 5-year gilt yields which increased by nearly 1.3% from 0.70% to 1.97%. 10-year gilt yields rose by nearly 1% ending the year at 2.73%. The increase was less pronounced for longer dated gilts; 20-year yields rose from 2.74% to 3.37% and 50-year yields rose from 3.23% to 3.44%. 3-month, 6-month and 12-month Libid rates remained at levels below 1% through the year.

## 5. THE HERITABLE BANK IMPAIRMENT

5.1 Heritable Bank (a UK financial institution) went into administration on 7th October 2008 as a direct result of its Icelandic parent Landbanki bank failing. The Authority held a £5 million deposit. This investment was made on 9th January 2008 for 364 days.

5.2 Since that date the Council has been vigorously chasing recovery of our funds and has lodged claims with the Heritable Bank administrator. Since this time the Authority has received regular distributions as set out below.

| **Table 1: Dividends received on Heritable Bank** | **Pence in the pound** | **£000s** |
|---|---|---|
| **Total received as at 31st March 2013** | **77.48** | **4,020** |
| Received August 2013 | 16.73 | 871 |
| **Total received as at 31st March 2014** | **94.21** | **4,891** |
| **Additional sum expected if High Court case is successful** | **5.79** | **301** |
| **Final sum including principal & full interest (sec 5.4)** | **100.00** | **5,192** |

5.3 In August 2013 following the sale of the Heritable mortgage book the Authority received a dividend of £871k (16.73), taking the total recovered to £4.9m (94.21p). We have now assumed there will no further payments from the Heritable administrators so have now written back the balance on the impairment to reserves , we had previously only assumed we would receive 87% of the total investment.

5.4 An announcement was made on 1st July 2014 that the administrators had agreed to pay the full dividend. This means the Authority has recovered all funds from the Heritable bank.

## 6 BORROWING IN 2013/14

6.1 The Council increased its overall borrowing by £4.4 million in loans ,including £3.5m of interest free loans to finance the Council's energy re-fit programme. The other loans were short term loans with an average interest rate of 0.45%.

6.2

| Table 2: Movement in year | Debt 1 April 2013 | Debt Repaid | New Debt Raised | Debt 31 March 2014 |
|---|---|---|---|---|
| | £000 | £000 | £000 | £000 |
| Temporary Borrowing (less than 12 mths.) | 29,000 | (33,000) | 37,000 | 33,000 |
| | **29,000** | **(33,000)** | **37,000** | **33,000** |
| Public Work Loan Board loans (PWLB) | 234,137 | (2,053) | - | 232,084 |
| Commercial Loan | 30,000 | - | - | 30,000 |
| Salix loan | 1,068 | (658) | 3,131 | 3,541 |
| | **265,205** | **(2,711)** | **3,131** | **265,625** |
| **Total Debt Outstanding** | **294,205** | **35,711** | **40,131** | **298,625** |

6.3 The Council's Treasury Management strategy continues to follow the same direction as it set since the financial collapse in October 2008, whereby capital expenditure is funded wherever possible by using the Council's internal cash reserves. This has a beneficial impact on the interest charges because of the large differential between long-term fixed borrowing and the interest rate in short term investments meant the 'cost of carry' would have been approximately 4%.

## 7. INTEREST ON TOTAL DEBT OUTSTANDING

7.1 The average rate paid on total external debt was in 2013/14 4.53% (4.63% 2012/13). The main impact was from low interest short term loans and from interest free loans from Salix to finance the Re-Fit Programme

7.2 Table 3 shows the interest paid (i.e. the cost of borrowing) by the Council during the year:

| Table 3: Cost of Borrowing | 2013/14 | 2012/13 |
|---|---|---|
| | £000 | £000 |
| Public Work Loan Board loans (PWLB) | 11,132 | 10,820 |
| Commercial Loan | 2,143 | 2,143 |
| Salix Loan | - | - |
| **Total Interest on Debt** | **13,275** | **12,963** |
| Short Term Loans | 136 | 142 |
| **Total interest paid** | **13,411** | **13,105** |
| Interest Premiums | - | 276 |

| Table 3: Cost of Borrowing | 2013/14 | 2012/13 |
|---|---|---|
| **Total Cost of Debt** | **13,411** | **13,381** |
| **Cost Attributed to the Housing Revenue Account** | 5,737 | 5,746 |
| **Cost Attributed to General Fund** | 7,674 | 7,635 |
| **Total Cost of Debt** | **13,411** | **13,381** |

7.3 The increase in interest relating to the PWLB reflects the full year effect of the £20 million of loans taken out at the end of March 2013.

## 8. DEBT MATURITY STRUCTURE

8.1 The Council has 33 loans spread over 47 years with the average maturity being 38 years. This maturity profile allows the Council to spread the risk of high interest rates when debt matures in any one year.

8.2 Table 4 shows the maturity structure of Enfield's long-term debt and the average prevailing interest rates.

| Table 4: Profile Maturing Debt | Debt Outstanding as at 31 March 2013 | Debt Outstanding as at 31 March 2014 |
|---|---|---|
| **Years** | **£m** | **£m** |
| Under 1 year | 31.3 | 36.1 |
| 1- 5 | 8.9 | 48.3 |
| 5-10 | 40.9 | 1.1 |
| 10-15 | 0 | 0 |
| 15-25 | 20.1 | 20.1 |
| 25-30 | 10.0 | 10.0 |
| 30-40 | 103.3 | 118.3 |
| 40+ | 79.8 | 64.8 |
| | **294.2** | **298.6** |

## 9. DEBT RESTRUCTURING

9.1 Debt restructuring normally involves prematurely replacing existing debt (at a premium or discount) with new loans in order to secure net savings in interest payable or a smoother maturity profile. Restructuring can involve the conversion of fixed rate interest loans to variable rate loans and vice versa.

9.2 No debt restructuring was undertaken during the year. We will continue to actively seek opportunities to re-structure debt over 2014/15.

## 10. TREASURY MANAGEMENT PRUDENTIAL INDICATORS: 2013/14

10.1 Throughout 2013/14 total loan debt was kept within the limits approved by the Council at its meeting in March 2014 against an authorised limit of £550 million and an operating limit of £400 million. The authorised limit (as defined by the Prudential Code) was set at £550 million as a precaution against the failure, for whatever reason, to receive a source of income e.g. Council Tax. In the unlikely event of this happening, the Council would need to borrow on a temporary basis to cover the shortfall in cash receipts. In practice it is the operating limit by which the Council monitors its borrowing; any significant breach must be reported to Council.

10.2 The Council held no variable interest rate debt during 2013/14. The Council's Prudential Code however does allow for up to 25% of the debt to be held in variable interest rate debt.

10.3 The Prudential code allows up to 25% of its debt to mature in one year (£75 million). This limit was not breached, the actual position as at 31 March 14 was £36.1m (12.1%).

## 11. INVESTMENTS

11.1 The Council manages its investments arising from cash flow activities in-house and invests within the institutions listed in the Authority's approved lending list. It can invest for a range of periods approved in the Annual Treasury Strategy Report. The Council acts as the treasury manager for the 79 Enfield schools within the HSBC banking scheme and Enfield Homes. The Council produces a three year cash flow model (based on daily transactions) which projects the cash flow movements of the Council linked into the Council's medium term financial plan. This allows the Treasury Management team to make more informed decisions on borrowing and lending.

11.2 In 2013/14 the Council received £0.6 million in interest on money lent out to the money markets an increase of £0.2 million from 2012/13. The average cash balance held by the Council during the year was £99 million (see Appendix 2) compared to £64 million in 2012/13. This is set out in table 5 below:

| **Table 5: Interest Receipts** | **2013/14 £000** | **2012/13 £000** |
|---|---|---|
| **Total Interest Receipts** | **541** | **412** |
| Interest paid to Enfield Homes | (5) | (6) |
| HRA balances | (26) | - |
| Section 106 Applications | (21) | (22) |
| Other Funds | (5) | (15) |
| **Total Interest to General Fund** | **484** | **369** |

11.3 Table 6 shows the maturity structure of Enfield's investments and the prevailing interest rates. The Authority continues to adopt a very prudent approach and but the 2013/14 strategy allowed investments up to 12 months with financial institutions that met our credit rating requirements (2012/13 only allowed to lend to approved financial institutions).

11.4

| **Table 6: Maturing Investments** | **Investments as at 31 March 2014** | **No of Deals** | **Investments as at 31 March 2013** | **No of Deals** |
|---|---|---|---|---|
| **Months** | **£000's** | | **£000's** | |
| On demand | 35,850 | 4 | 17,700 | 4 |
| Within 1 Month | 12,500 | 2 | - | - |
| Within 3 Months | 7,500 | 1 | 22,500 | 3 |

| Table 6: Maturing Investments | Investments as at 31 March 2014 | No of Deals | Investments as at 31 March 2013 | No of Deals |
|---|---|---|---|---|
| Within 6 Months | - | - | - | - |
| Within 9 Months | - | - | - | - |
| Within 12 Months | 7,500 | 1 | - | - |
| | **63,350** | **8** | **40,200** | **7** |

11.5 The Treasury Management team achieved an average interest rate of 0.55% (0.63% 12/13), out-performing the benchmark (Inter-Bank 7-day lending rate 0.43%). This was achieved by adopting an active treasury policy. The average interest rate fell due to banks reducing interest rates on our call accounts.

**Net Borrowing**

11.6 The Council's net borrowing decreased in 2013/14 as Table 7 demonstrates the cost of the Council's capital programme over the year. It recognised that future capital expenditure will need to be financed from external borrowing, will create pressure on the revenue budget but this impact as been recognised in the Council's Medium term financial plan.

| Table 7: Trend in Net Borrowing | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 |
|---|---|---|---|---|---|
| | **£000** | **£000** | **£000** | **£000** | **£000** |
| Total Borrowing | 220,347 | 218,347 | 264,136 | 294,204 | 298,624 |
| Total Investments | (74,150) | (30,000) | (43,600) | (40,200) | (63,350) |
| **Net Borrowing** | **146,197** | **188,347** | **220,536** | **254,004** | **235,274** |
| **Annual change in net debt** | **48,950** | **42,150** | **32,189** | **33,468** | **(18,730)** |

The Capital Financing Requirement reflects the Council's underlying need to borrow to fund its capital programme (Table 8).

| Table 8: Capital Financing Requirement (CFR) | 31st March 2014 | 31st March 2013 |
|---|---|---|
| | **£m's** | **£m's** |
| General Fund | 264.9 | 259.3 |
| Housing Revenue Account | 157.7 | 157.7 |
| **Total** | **422.6** | **417.0** |

The Council is allowed to borrow up to its capital financing requirement which means it has £124m headroom to increase it's borrowing.

11.7 Through careful cash management control (i.e. the ability to accurately predict the daily out/in flows of cash) the Treasury Management team have limited the Council's overdraft costs in the year to £96.

11.8 Going forward, the cost of the capital programme will increase over the next three years. It is helpful to note the increasing ratio of financing costs to net revenue stream in comparison to other London boroughs. This trend is shown in Appendix 3.

## 12. ALTERNATIVE OPTIONS CONSIDERED

12.1 None. This report is required to comply with the Council's Treasury Management Policy statement, agreed by Council in February 2013.

## 13. REASONS FOR RECOMMENDATIONS

13.1 To inform the Council of Treasury Management performance in the financial year 2013/14.

## 14. COMMENTS OF THE DIRECTOR OF FINANCE, RESOURCES, AND CUSTOMER SERVICES AND OTHER DEPARTMENTS

### 14.1 Financial Implications

Financial implications are set out in the body of the report.

### 14.2 Legal Implications

The Council has a statutory duty to ensure the proper administration of its financial affairs and a fiduciary duty to tax payers to use and account for public monies in accordance with proper practices.

The Statement has been prepared in accordance with the CIPFA Code of Practice.

### 14.2 Key Risks

Extending the maximum period of deposits will increase the level of risk of default. This fact must be considered against backdrop that investments will still be restricted to countries (outside of UK with a sovereign rating of AAA and that deposits will be made only with financial institutions with a high credit rating.

## 15. IMPACT ON COUNCIL PRIORITIES

### 15.1 Fairness for All

Effective financial management provides the basis for the Council to achieve its priorities and objectives. This report explains a key part of effective financial management and the progress that has been made during the year.

### 15.2 Growth and Sustainability

Effective financial management provides the basis for the Council to achieve its priorities and objectives. This report explains a key part of effective financial management and the progress that has been made during the year.

**15.3 Strong Communities**
Effective financial management provides the basis for the Council to achieve its priorities and objectives. This report explains a key part of effective financial management and the progress that has been made during the year.

## 16. PERFORMANCE MANAGEMENT IMPLICATIONS

**16.1** The report provides clear evidence of sound financial management, efficient use of resources, promotion of income generation and adherence to Best Value and good performance management.

## 17. EQUALITIES IMPACT IMPLICATIONS

**17.1** The Council is committed to Fairness for All to apply throughout all work and decisions made. The Council serves the whole borough fairly, tackling inequality through the provision of excellent services for all, targeted to meet the needs of each area. The Council will listen to and understand the needs of all its communities.

**17.2** Financial reporting and planning is important in ensuring resources are used to deliver equitable services to all members of the community.

## 18. PUBLIC HEALTH IMPLICATIONS

There are no public health implications directly related to this report.

Background Papers:
None

## APPENDIX 1: INVESTMENTS OUTSTANDING AT 31$^{ST}$ MARCH 2014

| Call Accounts | Amount lent (£000) | Interest rate | Maturity Date |
|---|---|---|---|
| HSBC | 3,850 | 0.40% | On demand |
| Santander | 12,500 | 0.40% | On demand |
| Handlesbanken | 12,500 | 0.60% | On demand |
| **Money Market Fund** | | | |
| Ignis | 7,000 | 0.38% | On demand |
| **Deposits** | | | |
| Barclays bank | 7,500 | 0.83% | 10$^{th}$ March 2015 |
| Lloyds bank | 7,500 | 0.75% | 22$^{nd}$ April 2014 |
| Lloyds bank | 5,000 | 0.75% | 7$^{th}$ May 2014 |
| Nationwide building society | 7,500 | 0.72% | 11$^{th}$ April 2014 |
| Total | **63,350** | | |

## APPENDIX 2:  Cash Flow Position 2013/14

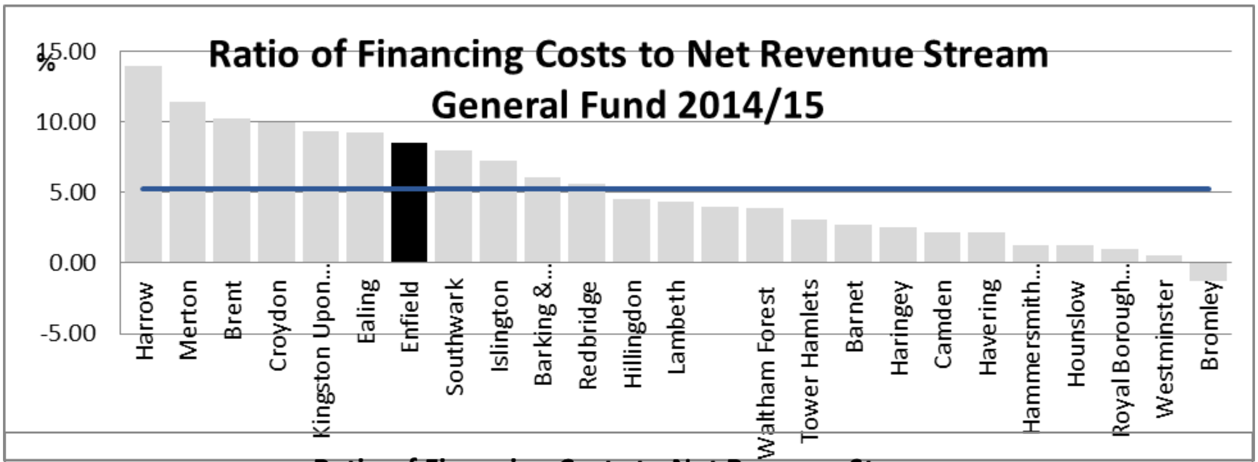
**2013/14**

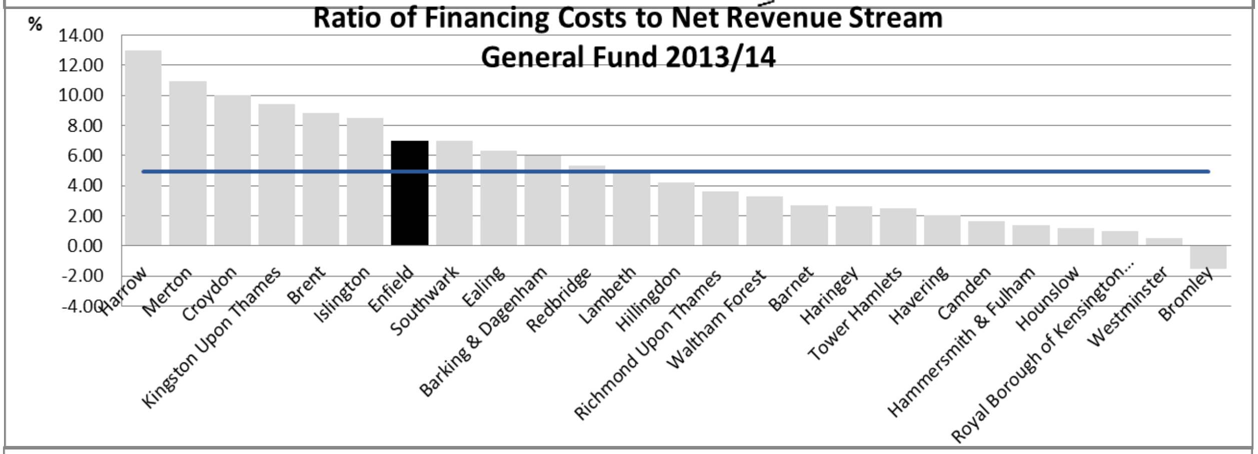
| | Average Balance *£'m* | days | Interest Earned *£'k* | **RETURN** |
|---|---|---|---|---|
| Apr-13 | 86.82 m | 30 | 40.3 k | 0.56% |
| May-13 | 123.37 m | 31 | 58.0 k | 0.55% |
| Jun-13 | 132.85 m | 30 | 60.5 k | 0.55% |
| Jul-13 | 125.68 m | 31 | 55.0 k | 0.52% |
| Aug-13 | 119.20 m | 31 | 52.6 k | 0.52% |
| Sep-13 | 105.69 m | 30 | 46.3 k | 0.53% |
| Oct-13 | 95.06 m | 31 | 43.0 k | 0.53% |
| Nov-13 | 98.03 m | 30 | 41.2 k | 0.51% |
| Dec-13 | 80.63 m | 31 | 38.1 k | 0.56% |
| Jan-14 | 76.85 m | 31 | 37.8 k | 0.58% |
| Feb-14 | 73.15 m | 28 | 33.0 k | 0.59% |
| Mar-14 | 71.14 m | 31 | 35.3 k | 0.58% |
| **Average/Total** | **99.18 m** | 365 | **541.2 k** | **0.55%** |

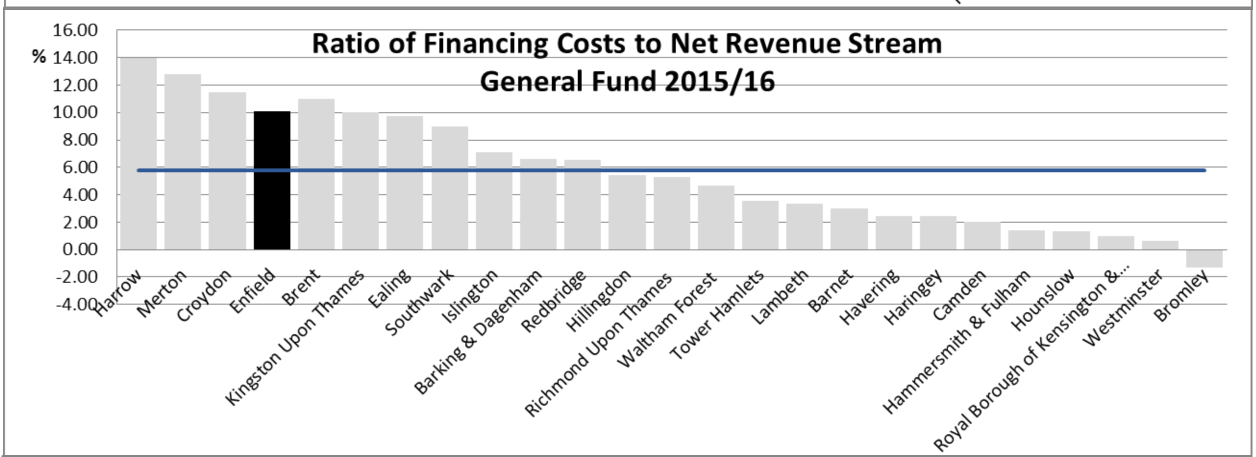
**Quarterly dates**

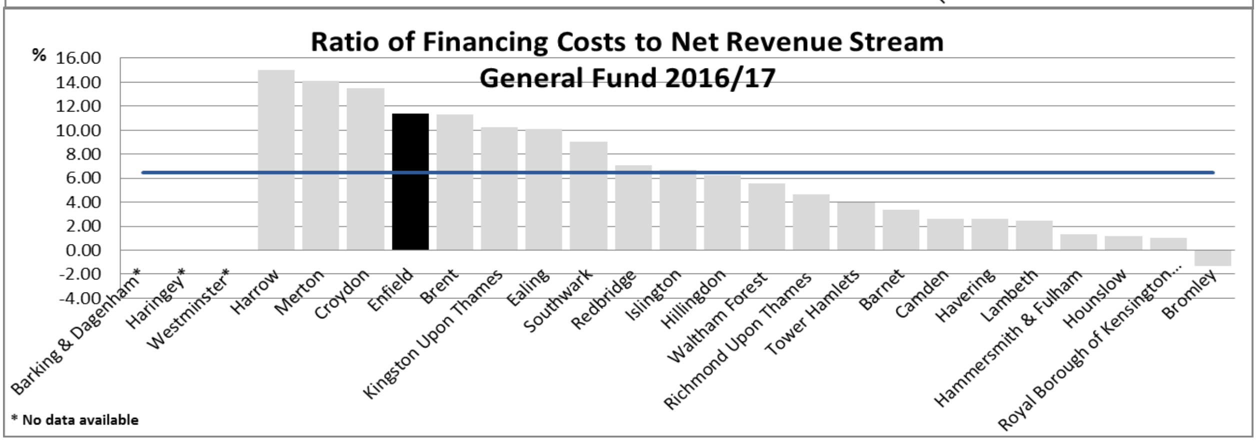
| | Balance Invested (£'m) |
|---|---|
| **31/03/2013** | 40.20 m |
| **30/06/2013** | 111.80 m |
| **30/09/2013** | 79.33 m |
| **31/12/2013** | 57.30 m |
| **31/03/2014** | 63.35 m |

**Appendix 3**


Ratio of Financing Costs to Net Revenue Stream
General Fund 2014/15
%
15.00
10.00
5.00
0.00
-5.00
Harrow
Merton
Brent
Croydon
Kingston Upon...
Ealing
Enfield
Southwark
Islington
Barking &...
Redbridge
Hillingdon
Lambeth
Waltham Forest
Tower Hamlets
Barnet
Haringey
Camden
Havering
Hammersmith...
Hounslow
Royal Borough...
Westminster
Bromley


Ratio of Financing Costs to Net Revenue Stream
General Fund 2013/14
%
14.00
12.00
10.00
8.00
6.00
4.00
2.00
0.00
-2.00
-4.00
Harrow
Merton
Croydon
Kingston Upon Thames
Brent
Islington
Enfield
Southwark
Ealing
Barking & Dagenham
Redbridge
Lambeth
Hillingdon
Richmond Upon Thames
Waltham Forest
Barnet
Haringey
Tower Hamlets
Havering
Camden
Hammersmith & Fulham
Hounslow
Royal Borough of Kensington...
Westminster
Bromley


Ratio of Financing Costs to Net Revenue Stream
General Fund 2015/16
%
16.00
14.00
12.00
10.00
8.00
6.00
4.00
2.00
0.00
-2.00
-4.00
Harrow
Merton
Croydon
Enfield
Brent
Kingston Upon Thames
Ealing
Southwark
Islington
Barking & Dagenham
Redbridge
Hillingdon
Richmond Upon Thames
Waltham Forest
Tower Hamlets
Lambeth
Barnet
Havering
Haringey
Camden
Hammersmith & Fulham
Hounslow
Royal Borough of Kensington &...
Westminster
Bromley


Ratio of Financing Costs to Net Revenue Stream
General Fund 2016/17
%
16.00
14.00
12.00
10.00
8.00
6.00
4.00
2.00
0.00
-2.00
-4.00
Barking & Dagenham*
Haringey*
Westminster*
Harrow
Merton
Croydon
Enfield
Brent
Kingston Upon Thames
Ealing
Southwark
Redbridge
Islington
Hillingdon
Waltham Forest
Richmond Upon Thames
Tower Hamlets
Barnet
Camden
Havering
Lambeth
Hammersmith & Fulham
Hounslow
Royal Borough of Kensington...
Bromley
* No data available