NOTTINGHAMSHIRE
Fire & Rescue Service
Creating Safer Communities

Nottinghamshire and City of Nottingham
Fire and Rescue Authority

TREASURY MANAGEMENT ANNUAL REPORT 2017/18

Report of the Treasurer to the Fire Authority

Date: 28 September 2018

Purpose of Report:

To provide Members with an update on treasury management activity during the 2017/18 financial year.

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1. BACKGROUND

1.1 Treasury management is defined as:

"The management of the organisation's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with these activities; and the pursuit of optimum performance consistent with those risks."

1.2 The Fire Authority 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 2017/18. The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised in 2017) was adopted by the Fire Authority on 9 April 2010.

1.3 The primary requirements of the Code are as follows:

1. The creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Authority's treasury management activities.

2. The creation and maintenance of treasury management practices which set out the manner in which the Authority will seek to achieve those policies and objectives.

3. Receipt by the Fire Authority of an annual Treasury Management Strategy Statement for the year ahead, a mid-year review report and an annual report covering activities during the previous year.

4. Delegation by the Authority of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

5. Delegation by the Authority of the role of scrutiny of the Treasury Management Strategy and policies to a specific named body. For this Authority, the delegated body is the Finance and Resources Committee.

1.4 This annual report has been prepared in compliance with CIPFA's Code of Practice, and covers the following:

- An economic review of 2017/18;

- A review of capital activity during 2017/18 and the impact of this on the Authority's capital financing requirement (CFR);

- A review of the Investment and Cash Management Strategy during 2017/18;

- Investment and cash activity during 2017/18;
- A review of the year end investments and cash position and usable reserves;
- A review of the Borrowing Strategy and borrowing activity during 2017/18;
- A summary of compliance with treasury and prudential limits for 2017/18.

1.5 The Authority has appointed Link Asset Services as its external treasury management adviser.

2. REPORT

ECONOMIC REVIEW

2.1 Following a period of relatively strong growth in the latter half of 2016, growth in the first half of 2017 was the slowest since 2012. The main reason for this was the sharp increase in inflation caused by the devaluation of sterling after the EU referendum, which increased the cost of imports. This caused a reduction in consumer disposal income and spending power as inflation exceeded average wage increases. Consequently, the services sector of the economy saw weak growth as consumers responded by cutting back on their expenditure. Growth did pick up modestly in the second half of 2017, raising market expectations of a rise in the bank rate. The bank rate was increased from 0.25% to 0.50% in November 2017. The minutes of the February meeting of the Monetary Policy Committee contained warnings of a faster pace of increases in bank rate than had previously been expected. Market expectations for increases in bank rate therefore shifted considerably during the second half of 2017/18 and this resulted in investment rates for durations of three to twelve months increasing sharply during the final quarter of the financial year.

2.2 Public Works Loan Board (PWLB) borrowing rates increased correspondingly to the developments around bank rate, with the shorter-term rates increasing more sharply than the longer term rates.

2.3 The major political event of the year was the UK general election on 8 June. However, this had relatively little impact on the financial markets.

REVIEW OF CAPITAL ACTIVITY IN 2017/18

2.4 The Authority undertakes capital expenditure on long term assets. These activities may either be:

- Financed immediately by way of capital or revenue resources (capital receipts, capital grants, revenue contributions), which does not give rise to a requirement to borrow; or

- If insufficient financing is available, or if a decision is taken not to apply resources, the capital expenditure will need to be financed by borrowing.

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

	2016/17 Actual	2017/18 Revised Budget	2017/18 Actual
	£000's	**£000's**	**£000's**
Capital Expenditure	**2,048**	**6,174**	**4,060**
Resourced By:			
- Capital Grants	6	371	25
- Capital Receipts	2,042	477	630
- Revenue Contributions	0		
- Internally Financed	0		
- Borrowing	0	5,326	3,405
Total Financed Capital Expenditure	**2,048**	**6,174**	**4,060**

2.6 The 2017/18 capital programme underspent and was well within the budget. As at 31 March 2018, the Authority's capital financing requirement was £26,278k, which was within the prudential indicator set of £28,407k. The CFR figure represents the Authority's underlying need to borrow to fund capital expenditure and equates to un-financed capital expenditure which has not yet been paid for by revenue funding or other resources such as capital grants or receipts. The CFR is reduced over time by way of a statutory minimum revenue provision charge to revenue which effectively charges the revenue budget for the use of capital assets over their asset lives.

REVIEW OF THE INVESTMENT AND CASH MANAGEMENT STRATEGY

2.7 The Treasury Management Strategy approved by the Authority set out the policies for managing investments and for giving priority to the security and liquidity of those investments. The risk appetite of this Authority is low in order to give priority to security of its investments. Accordingly, the following types of low risk specified investments may be made:

- Deposits with the Debt Management Agency (Government);
- Term deposits with banks and building societies;
- Term deposits with uncapped English and Welsh local authority bodies;
- Call deposits with banks and building societies;
- Triple-A rated Money Market Funds;
- UK Treasury Bills;
- Certificates of Deposit.

During the year, all investments were made with banks, building societies (either term deposits or call deposits) and other local authority bodies.

2.8 The Authority will aim to limit its investment with any single counterparty to £2m, although the strategy noted that this was sometimes difficult to achieve. No term deposits will be made for more than one year without the prior approval of the Treasurer and the Chair of Finance and Resources Committee. The selection of counterparties with a high level of creditworthiness will be achieved by reference to Link's weekly credit list of potential counterparties. The Link weekly credit list shows potential investment counterparties, which are colour-coded to indicate the maximum period it is recommended that investments are made for. The Authority will therefore use counterparties with the following durational colour codes:

- Blue - investments up to one year (only applies to nationalised or semi nationalised UK banks);
- Orange – investments up to one year;
- Red – investments up to six months;
- Green – investments up to 100 days.

The Authority has made all investments with counterparties during the year in accordance with the maximum periods advised by Link.

2.9 The Authority will avoid locking into longer term deals while investment rates are at such low levels unless exceptionally attractive rates are available which make longer term deals seem worthwhile.

2.10 In terms of cash resources, the strategy is to maintain a bank overdraft facility of £200,000, to continue to use cash flow forecasting to predict cash surpluses and shortfalls so that these can be managed and to invest current account balances in the business premium account on a daily basis if the interest rate is favourable.

2.11 All aspects of the Treasury Management Strategy outlined for 2017/18 remained in place throughout the year. The Strategy included a forecast for the bank rate, which showed that this was expected to be at 0.25% by 31 March 2018. As stated in Paragraph 2.1, the bank rate was actually increased to 0.50% in November 2017.

INVESTMENT AND CASH ACTIVITY IN 2017/18

2.12 As at 31 March 2018, the Authority held £9.050m of principal as short term investments. This comprised eight separate investments with five different counterparties. All of the investments were for £2m or less. Six of the investments were call accounts held with four different banks and one building society, and one was a fixed term deposit with Barclays Bank. The fixed term deposit was for 95 days and it matured in June 2018. Of the six call accounts held at the end of 2017/18, all are still in place with their balances unchanged at the time of writing this report.

2.13 During the course of the year, three new investments were made, excluding the overnight sweep to the business premium account. All investments were made in accordance with the Authority's credit rating criteria policy. Due to difficulties in placing funds with counterparties that met the credit rating criteria, the Authority invested a total of £8.5m in two separate Barclays call accounts in August 2017 following the receipt of the £9.9m pension fund top up grant. £7m of this has subsequently been withdrawn.

2.14 Of the six call accounts held at 31 March 2018, five had been held for more than one year. These accounts had notice periods ranging from one day to 185 days. All counterparties have their creditworthiness continually monitored against Link's credit listings, and had it looked likely that the maximum recommended investment term for these institutions would have fallen below the call account notice period, then the funds would have been withdrawn.

2.15 The three month LIBID benchmark rate for the year was 0.2861%. The Authority's investments earned an average rate of 0.45% during the year resulting in total investment (including overnight savings interest on the current account) income earned of £40k, against a budgeted sum for investment income of £66k.

2.16 There was no requirement to use the Authority's overdraft facility during the year.

REVIEW OF INVESTMENTS/CASH POSITION AND USABLE RESERVES

2.17 Members will be aware that the Authority's "usable" reserves – ie: the general fund and earmarked reserves have not been fully cash backed in the past due to the use of cash balances to support capital expenditure in previous years. This strategy of using internally borrowed funds is considered prudent as investment returns are low and counterparty risk is still an issue.

2.18 At 31 March 2018 the value of the Authority's usable reserves totalled £12.456m. The balance sheet as at the same date shows that short term investments were valued at £7.436m and cash and cash equivalents held totalled £2.005m. This means that reserves are not fully cash-backed to the tune of £3.015m, a figure which has decreased from £4.015m at the end of 2016/17. The 2017/18 Treasury Management Strategy set out the Authority's aim to reduce the level of internal borrowing and build up cash balances to ensure that usable reserves are cash-backed to an appropriate level, however the Strategy also made it clear that the timing and rate at which cash balances increased would very much depend on the prevailing economic conditions. Opportunities have arisen during the year for the Authority to borrow from PWLB at relatively low interest rates, and this has allowed the level of internal borrowing to be reduced whilst minimising the "cost of carry" that arises due the differential between borrowing and investment rates. The average rate for a 25 year PWLB maturity loan was 2.69% during 2017/18, whilst the average rate of return on investments was 0.45%. The Authority has therefore saved around 2.24% through the use of internal borrowing. This equates to £67.5k on a balance of £3.015m.

Members can be assured that if the Authority needs to spend some of its usable reserves there is sufficient liquidity in its financial position to enable it to do so.

REVIEW OF THE BORROWING STRATEGY AND BORROWING ACTIVITY IN 2017/18

2.19 The strategy recommended that a combination of capital receipts, internal funds and borrowing would be used to finance capital expenditure during 2017/18. Capital receipts of £630k and capital grant of £25k were applied to finance expenditure.

2.20 The Authority has taken out three short term loans throughout the year:

£2.5m from the London Borough of Newham for 20 days at a rate of 0.25%
£1.2m from Nottinghamshire County Council for 10 days at a rate of 0.38%,
and £2m from Nottinghamshire County Council for 10 days at rate of 0.75%.

The total interest cost of these loans was £1.9k including administration and brokerage fees. These loans were taken to fill short term gaps in the Authority's cash flow.

2.21 In December 2017, the Authority took two PWLB maturity loans: £1m for 9.5 years at a rate of 1.96% and £1m for 50 years at a rate of 2.30%. This provided a "blended" rate of 2.13% over an average duration of approximately 30 years, which compared favourably with the equivalent rates for 30 year EIP and annuity loans (2.37% and 2.42% respectively). These loans reduced the Authority's average long term borrowing rate from 3.65% to 3.52%, and reduced the Authority's level of internal borrowing.

2.22 The treasury management limits to loan maturity were set in 2017/18 and are shown below:

Loan Maturity		
	Upper Limit	**Lower Limit**
Under 12 months	20%	0%
12 months to 5 years	30%	0%
5 years to 10 years	75%	0%
10 years to 20 years	100%	0%
Over 20 years	100%	30%

2.23 No rescheduling of debt took place, as the differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

2.24 The authorised limit is the affordable borrowing limit above which the Authority does not have the power to borrow. This was set at £30.538m for 2017/18. Total external debt as at 31 March 2018 was £25.183m, which was well within the authorised limit.

2.25 The operational boundary is the expected borrowing position of the Authority within the year. This was set at £27.762m for 2017/18, and was not exceeded at any point during the year.

SUMMARY OF COMPLIANCE WITH TREASURY AND PRUDENTIAL LIMITS

2.26 The following indicators were approved by Members for the 2017/18 financial year. Actual performance is shown in the final column of the table below:

Treasury or Prudential Indicator or Limit	Approved for 2017/18	Actual for 2017/18
Estimate of Ratio of Financing Costs to Net Revenue Stream	6.0%	5.5%
Estimate of the Incremental Impact of New Capital Investment Decisions on the Council Tax (Band D)	£0.40	£0.40
Estimate of Total Capital Expenditure to be Incurred	£5,113,000	£4,060,000
Estimate of Capital Financing Requirement	£28,407,000	£26,278,000
Operational Boundary	£27,762,000	Not exceeded
Authorised Limit	£30,538,000	Not exceeded
Upper limit for fixed rate interest exposures	100%	100%
Upper limit for variable rate interest exposures	30%	0%
Loan Maturity:	Limits:	Limits:
Under 12 months	Upper 20% Lower 0%	17.9%
12 months to 5 years	Upper 30% Lower 0%	19.0%
5 years to 10 years	Upper 75% Lower 0%	4.0%
10 years to 20 years	Upper 100% Lower 0%	0.0%
Over 20 years	Upper 100% Lower 30%	59.2%
Upper Limit for Principal Sums Invested for Periods Longer than 365 Days	£2,000,000	£2,000,000

2.27 The indicator for the ratio of financing costs to net revenue stream shows an actual result of 5.5% compared to an estimated ratio of 6.0%. This is partly due to the actual financing costs being £181k lower than estimated, and partly due to the net revenue stream being £302k higher than estimated. Interest costs underspent by £117k due to a combination of borrowing later than planned, as well as borrowing at a lower rate than budgeted. The minimum revenue provision charge underspent by £91k, which was due to capital expenditure for 2016/17 (on which the 2017/18 charge is based) being lower than originally anticipated due to a significant amount of capital expenditure being slipped into 2017/18. The higher revenue stream is due to that fact that the calculation of the indicator was based on provisional tax base figures which were lower than the actual figures, and budgeted grant figures that were lower than the actual amount received.

2.28 The indicator for the incremental impact of new capital investment decisions on Council Tax shows an actual result of £0.40, which is in line with the estimate.

3. FINANCIAL IMPLICATIONS

The financial implications of this report are set out in full within the body of the report.

4. HUMAN RESOURCES AND LEARNING AND DEVELOPMENT IMPLICATIONS

There are no human resources or learning and development implications arising from this report.

5. EQUALITIES IMPLICATIONS

An equality impact assessment has not been undertaken because this report gives a review of activities rather than introducing a new policy.

6. CRIME AND DISORDER IMPLICATIONS

There are no crime and disorder implications arising directly from this report.

7. LEGAL IMPLICATIONS

There are no legal implications arising directly from this report, other than the requirement to act within the Authority's powers when undertaking treasury management borrowings and investments.

8. RISK MANAGEMENT IMPLICATIONS

Risk management is a key aspect of treasury management, and the Treasury Management Strategy sets out the parameters within which activities will be carried out with a view to managing credit risk, liquidity risk, re-financing risk and market risk. The Authority has approved a prudent approach to treasury management and this report allows Members to review how well risks have been managed during the year.

9. COLLABORATION IMPLICATIONS

There are no collaboration implications arising from this report.

10. RECOMMENDATIONS

That Members note the contents of this report.

11. BACKGROUND PAPERS FOR INSPECTION (OTHER THAN PUBLISHED DOCUMENTS)

None.

Charlotte Radford
TREASURER TO THE FIRE AUTHORITY