REPORT TO:	Executive Board
DATE:	25 February 2016
REPORTING OFFICER:	Operational Director – Finance
PORTFOLIO:	Resources
TITLE:	Treasury Management Quarter 3 2015/16
WARDS:	Borough-wide

1.0 PURPOSE OF REPORT

1.1 The purpose of this report is to provide an update regarding activities undertaken on the money market as required by the Treasury Management Policy.

2.0 RECOMMENDED: That the report be noted.

3.0 SUPPORTING INFORMATION

Economic Outlook

3.1 The following analysis of the economic situation has been provided by Capita Asset Services, the Council's treasury management advisors.

3.2 During the quarter ended 31 December 2015:

- The economic recovery regained some momentum during Q4 2015 after a disappointing Q3 2015
- Household spending growth strengthened
- Wage growth slowed despite further falls in unemployment
- The UK came out of its brief dip into deflation
- The prospect of a rate hike before mid-2016 remained unlikely
- The Federal Reserve made a start in raising interest rates, and the European Central Bank (ECB) loosened policy
- The Chancellor smoothed out his fiscal austerity plans over the term of this Parliament

3.3 The economic recovery was shown to have slowed by more than previously thought, with real Gross Domestic Product (GDP) growth decelerating from 0.5% in quarter 2 to 0.4% in quarter 3. The annual growth rate in quarter 3 was also revised down from 2.3% to 2.1%. The revisions were driven largely by weaker contributions from investment expenditure.

3.4 The latest survey evidence and official monthly data suggest that the recovery picked up pace again during the final quarter of 2015. In addition to the CBI's Composite Growth Indicator pointing to greater economic expansion in quarter 4 of 2015, the Markit/CIPS composite Purchasing Managers Indicators (PMI) are consistent with quarterly GDP growth strengthening to about 0.6%, which would imply 2.2% GDP growth in 2015 as a whole. Quarter 3's unusually weak contribution of construction output to overall GDP is also likely to have been reversed by the end of 2015.

3.5 Consumer spending will probably have provided a significant boost, given that retail sales experienced what was almost certainly their strongest quarter this year. Spending off the high street looks to have fared well too, in part owing to consumer confidence remaining high. Survey measures such as the CBI's consumer services business volumes balance indicate that annual growth in real household spending on consumer services could have risen in the quarter, from 1.6% to as much as 3%.

3.6 The jobs recovery pressed on, as employment rose by 176,000, and by a further 91,000 in October, pushing the employment rate up to a record-high. Consequently, the International Labour Organisation (ILO) unemployment rate was driven down for four successive months between July and October, from 5.6% to 5.2% – a level not far above some estimates of its natural rate. However, by taking a wider perspective on labour market slack, we do not believe the labour market is as tight as these data alone suggest. First, impressive jobs growth reflected large increases in self-employment, as well as significant numbers of new part-time jobs, rather than conventional full-time placements. Moreover, the percentage of those in part-time work wanting to work extra hours in a full-time role saw the largest upturn for 2½ years in October, and the proportion of temporary workers wanting permanent positions has been on the rise throughout the second half of the year. Meanwhile, employer surveys have shown that recruitment difficulties have either held steady or eased recently. It is, therefore, not too surprising that pay growth has weakened so much of late. Annual growth in regular pay (ex. bonuses) reduced to 1.9%, in contrast to 2.5% in the previous quarter.

3.7 These labour market figures will have reassured the Monetary Policy Committee (MPC) doves that inflationary pressures remain muted, thereby reinforcing expectations that a rate rise is still some way off. Only recently the newest MPC member, stressed that he needs to see a decisive acceleration of wage growth before considering voting for a rate hike. And weak inflationary pressures from the labour market have been compounded by renewed falls in the energy prices in reinforcing the case to keep rates on hold for a while yet.

The sterling price of Brent Crude fell below £24 per barrel in December, and wholesale gas and electricity prices fell further too. While it looks like the UK's brief flirtation with deflation in 2015 came to an end in November – CPI inflation nudged back into positive territory at 0.1% – inflation will remain below target for a long while yet. Despite these disinflationary pressures, inflation will pick up in coming months as the previous, (sharper), falls in oil prices will drop out of the calculation of the annual figure.

3.8 Turning to the public finances, the Chancellor delivered his Spending Review and Autumn Statement in November. Due to the OBR "finding" another £27bn of savings over the forecast period, from changing various forecasts and modelling assumptions, Mr Osborne was allowed to reverse his tax credits cuts, and to pursue a more balanced path of consolidation over the parliament. But while the profile and pace of cuts have eased a little, the intensity of the consolidation package as a whole is not that different to the one presented in July's Budget, and remains far more austere than those faced in other advanced economies. The OBR forecasts that Mr Osborne will achieve a £10bn budget surplus in 2019-20 and that net debt as a percentage of GDP will fall in every year of the Parliament.

3.9 However, November's public finance figures now indicate that an overshoot of the borrowing target for this fiscal year is likely. On the other hand, since we think the OBR is too cautious about the scope for productivity and GDP growth to bounce back, it is quite possible that the Chancellor actually ends up reaching his £10bn budget surplus earlier than the current OBR forecast.

3.10 Finally, the FTSE 100 rose by 3% between end-Q3 and end-Q4. However, UK equity prices were still down by 5% over the year as a whole. By comparison, global equities rose over 4% and fell by 4.5% over 2015 as a whole. Meanwhile, on a trade-weighted basis, sterling weakened by around 0.4%. This left it around 3% higher than the start of the year.

Interest Rate Forecast

3.11 The following forecast has been provided by Capita Asset Services.

	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Bank rate	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.50%	1.50%	1.75%	1.75%	2.00%	2.00%	2.00%
5yr PWLB rate	2.40%	2.60%	2.70%	2.80%	2.80%	2.90%	3.00%	3.20%	3.30%	3.40%	3.50%	3.50%	3.60%
10yr PWLB rate	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	4.10%	4.10%
25yr PWLB rate	3.70%	3.80%	3.90%	4.00%	4.10%	4.10%	4.20%	4.30%	4.30%	4.40%	4.40%	4.40%	4.50%
50yr PWLB rate	3.60%	3.70%	3.80%	3.90%	4.00%	4.00%	4.10%	4.20%	4.20%	4.30%	4.30%	4.30%	4.40%

Short Term Borrowing Rates

3.12 The bank base rate remained at 0.50% throughout the quarter.

		Oct		Nov		Dec	
	Start	Mid	End	Mid	End	Mid	End
	%	%	%	%	%	%	%
Call Money (Market)	0.48	0.48	0.48	0.48	0.48	0.48	0.45
1 Month (Market)	0.51	0.51	0.51	0.51	0.50	0.50	0.50
3 Month (Market)	0.58	0.58	0.58	0.57	0.57	0.58	0.59

Longer Term Borrowing Rates

		Oct		Nov		Dec	
	Start	Mid	End	Mid	End	Mid	End
	%	%	%	%	%	%	%
1 Year (Market)	1.04	1.02	1.04	1.03	1.03	1.06	1.07
10 Year (PWLB)	2.62	2.60	2.78	2.83	2.69	2.74	2.85
25 Year (PWLB)	3.30	3.35	3.46	3.49	3.37	3.38	3.50

3.13 Market rates are based on LIBOR rates published at the middle and end of each month. PWLB rates are for new loans based on principal repayable at maturity.

Borrowing and Investments

Turnover During the Period

	No of deals	Turnover £m
Short Term Borrowing	-	-
Short Term Investments	4	30

Position at Month End

	Oct £m	Nov £m	Dec £m
Total Borrowing	168	168	168
Total Investments	(183)	(183)	(183)
Call Account Balance	(23)	(25)	(18)

Investment Benchmarking

Benchmark	Benchmark Return %	Performance Oct - Dec %	Investment Interest Earned £000
7 day	0.36	0.48	28
1 month	0.38	0.00	-
3 month	0.45	0.87	33
6 month	0.61	0.72	97
12 month	0.92	0.76	216
Total			**374**

3.14 This shows the Council has over achieved the benchmark for most maturities for the last quarter. Due to the Council's strict treasury management guidelines only Counterparties with a very high credit score can be used for 12 months investments. For this reason returns are not as high as the benchmark return.

Budget Monitoring

	Net Interest at 31st December 2015				
	Budget Year to Date £000	**Actual Year to Date £000**	**Variance (o/spend) £000**		**Actual inc M Gateway £000**
Investment	(291)	(566)	275		(1,153)
Borrowing	1,145	1,178	(34)		4,470
Total	**854**	**612**	**242**		**3,317**

3.15 As the borrowing and investments in relation to the Mersey Gateway scheme are to be capitalised they will have no effect on the revenue budget and have therefore been excluded from the budget monitoring figures above.

New Long Term Borrowing

3.16 No new loans have been taken in this quarter.

Policy Guidelines

3.17 The Treasury Management Strategy Statement (TMSS) for 2015/16, which includes the Annual Investment Strategy, was approved by the Council on 04 March 2015. It sets out the Council's investment priorities as being:

- Security of capital;
- Liquidity; and
- Yield

3.18 The Council will also aim to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity. In the current economic climate and the heightened credit concerns it is considered appropriate to keep the majority of investments short term and to ensure all investments are in in line with Sector's credit rating methodology.

Treasury Management Indicators

3.19 It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators were set out in the Treasury Management Strategy Statement and are reviewed in Appendix 1.

Debt Rescheduling

3.20 No debt rescheduling was undertaken during the quarter.

4.0 POLICY IMPLICATIONS

4.1 None.

5.0 FINANCIAL IMPLICATIONS

5.1 The financial implications are as set out in the report.

6.0 IMPLICATIONS FOR THE COUNCIL'S PRIORITIES

6.1 There are no direct implications, however, the revenue budget and capital programme support the delivery and achievement of all the Council's priorities.

7.0 RISK ANALYSIS

7.1 The main risks with Treasury Management are security of investment and volatility of return. To combat this, the Authority operates within a clearly defined Treasury Management Policy and annual borrowing and investment strategy, which sets out the control framework

8.0 EQUALITY AND DIVERSITY ISSUES

8.1 None.

9.0 LIST OF BACKGROUND PAPERS UNDER SECTION 100D OF THE LOCAL GOVERNMENT ACT 1972

9.1 There are no background papers under the meaning of the Act.

Appendix 1

Treasury and Prudential Indicators – 2015/16 - Quarter 3

	2014/15	2015/16	
Prudential Indicators	**Full Year Actual £000**	**Original Estimate £000**	**Quarter 3 Estimate £000**
Capital Expenditure	32,157	40,202	47,987
Net Financing Need for the Year *(Borrowing Requirement)*	3,787	23,404	17,179
Increase / (Decrease) in CFR *(Capital Financing Requirement)*	853	20,208	14,354
Ratio of Financing Costs to Net Revenue Stream *(Proportion of cost of borrowing to Council's net revenue)*	2.9%	3.4%	2.9%
Incremental Impact on band D Council Tax (£) *(net cost of borrowing compared to tax base)*	8.19	17.21	2.07
External Debt	183,000	153,000	153,000
Operational Boundary *(Limit of which external debit is not epected to exceed)*	252,600	255,313	255,313
Authorised Limit *(Limit beyound which external debit is prohibited)*	270,000	270,000	270,000

Upper Limit for Interest Rate Exposure	**Exposure Limit %**	**2014/15 Actual %**	**2015/16 Estimate %**
Fixed Rate	100	100	88
Variable Rate	30	-	12

Maturity Structure of Fixed Rate Borrowing	**Exposure Limit %**	**2014/15 Actual %**	**2015/16 Estimate %**
Under 12 months	40	16	15
12 months to 24 months	40	5	6
24 months to 5 years	40	5	0
5 years to 10 years	40	0	0
10 years and above	100	73	79

Maximum Principal invested > 365 days	Investment Limit £000	2014/15 Actual £000	2015/16 Estimate £000
Principal Sums Invested over 365 days	30,000	10,000	10,000