Title of meeting:	Governance and Audit and Standards Committee Cabinet City Council
Date of meeting:	Governance and Audit and Standards Committee 16 September 2016 Cabinet 22 September 2016 City Council 11 October 2016
Subject:	Treasury Management Outturn Report 2015/16
Report by:	Director of Finance and Information Services (Section 151 Officer)
Wards affected:	All
Key decision:	No
Full Council decision:	Yes

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1. Purpose of report

The Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code requires local authorities to calculate prudential indicators before the start of and after each financial year. Those indicators that the Council is required to calculate at the end of the financial year are contained in Appendix A of this report.

The CIPFA Code of Practice on Treasury Management also requires the Section 151 Officer to prepare an annual report on the outturn of the previous year. This information is shown in Appendix B of the report.

2. Recommendations

That the following recommendations relating to Appendices A and B of this report be approved:

Appendix A - that the following actual prudential indicators based on the unaudited draft accounts be noted:

(a) The actual ratio of non-Housing Revenue Account (HRA) financing costs to the non HRA net revenue stream of 11.9%;

(b) The actual ratio of HRA financing costs to the HRA net revenue stream of 13.1%;

(c) Actual non HRA capital expenditure for 2015/16 of £115,276,000;

(d) Actual HRA capital expenditure for 2015/16 of £27,437,000;

(e) The actual non HRA capital financing requirement as at 31 March 2016 of £280,516,000;

(f) The actual HRA capital financing requirement as at 31 March 2016 of £154,734,000;

(g) Actual external debt as at 31 March 2016 was £490,378,035 compared with £462,566,096 at 31 March 2015.

Appendix B - That the following actual Treasury Management indicators for 2015/16 be noted:

(a) The Council's gross debt less investments at 31 March 2016 was £118,551,000;

(b) The maturity structure of the Council's borrowing was

	Under 1 Year	1 to 2 Years	3 to 5 Years	6 to 10 Years	11 to 20 Years	21 to 30 Years	31 to 40 Years	41 to 50 Years
Actual	1%	1%	2%	4%	18%	10%	22%	42%

(c) The Council's sums invested for periods longer than 364 days at 31 March 2016 were:

	Actual £m
31/3/2016	196
31/3/2017	106
31/3/2018	33

(d) The Council's fixed interest rate exposure at 31 March 2016 was £220m, ie. the Council had net fixed interest rate borrowing of £220m

(e) The Council's variable interest rate exposure at 31 March 2016 was (£186m), ie. the Council had net variable interest rate investments of £186m

3. Background

The Local Government Act 2003 requires local authorities to have regard to the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code for Capital Finance in Local Authorities.

The Prudential Code requires local authorities to adopt the CIFPA Code of Practice for Treasury Management in the Public Sector, which the City Council originally adopted in April 1994. Under the Code of Practice for Treasury Management an Annual Policy Statement is prepared setting out the strategy and objectives for the coming financial year. The Council approved the policy statement for 2015/16 on 17 March 2015. The Council approved the following revisions to the policy statement on 10 November 2015:

- Changing the method of calculating the minimum revenue provision (MRP) for the repayment of debt for post 1 April 2008 self-financed General Fund borrowing (with the exception of finance leases, service concessions and borrowing to fund long term debtors) from the equal instalment of principal method to the annuity method effect from 2015/16
- To allow investments to be made in enhanced or cash plus money market funds on the basis of a single credit rating
- Some investment counter party limits were revised to reflect changes to credit ratings

The Code of Practice also requires the Section 151 Officer to prepare an annual report on the outturn of the previous year. This information is shown in Appendix B of the report.

This report is based on the Council's unaudited draft accounts as the audit is not due to be completed until the end of September. Basing the report on the unaudited draft accounts will enable the report to be considered in the September / October meeting cycle rather than in November.

4. Reasons for Recommendations

The net cost of Treasury Management activities and the risks associated with those activities have a significant effect on the City Council's overall finances.

5. Legal implications

The Section 151 Officer is required by the Local Government Act 1972 and by the Accounts and Audit Regulations 2011 to ensure that the Council's budgeting, financial management, and accounting practices meet the relevant statutory and professional requirements. Members must have regard to and be aware of the wider duties placed on the Council by various statutes governing the conduct of its financial affairs.

6. Director of Finance & Information Services (Section 151 Officer) comments

All financial considerations are contained within the body of the report and the attached appendices

…………………………………………………………………….
Signed by Director of Finance & Information Services (Section 151 Officer)

Appendices:

Appendix A: Prudential Indicators
Appendix B: Treasury Management Outturn

Background list of documents: Section 100D of the Local Government Act 1972

The following documents disclose facts or matters, which have been relied upon to a material extent by the author in preparing this report:

	Title of document	**Location**
1	Information pertaining to the treasury management outturn	Financial Services
2		

The recommendation(s) set out above were approved/ approved as amended/ deferred/ rejected by the Cabinet on 22 September 2016.

………………………………………………
Signed by: the Leader of the Council

APPENDIX A

ACTUAL PRUDENTIAL INDICATORS

1. RATIO OF FINANCING COSTS TO NET REVENUE STREAM 2015/16

This ratio reflects the annual cost of financing net debt as a proportion of the total revenue financing received. It therefore represents the proportion of the City Council's expenditure that is largely fixed and committed to repaying debt. The higher the ratio, the lower the flexibility there is to shift resources to priority areas and/or reduce expenditure to meet funding shortfalls.

For the General Fund, this is the annual cost of financing debt and as a proportion of total income received from General Government Grants, Non Domestic Rates and Council Tax. The ratios of financing costs to net revenue streams for the General Fund in 2015/16 were as follows:

	Original Estimate	**Actual**
	£'000	£'000
Financing Costs:		
Interest Payable	17,100	17,790
Interest Receivable	(2,244)	(3,858)
Provision for Repayment of Debt	7,018	6,335
Total Financing Costs	**21,874**	**20,267**
Net Revenue Stream	**167,190**	**169,893**
Ratio of Financing Costs to Net Revenue Stream	**13.1%**	**11.9%**

Interest payable was £0.7m more than the original estimates. The Council borrowed £33m in 2015/16 which had not been included in the original estimates in order to take advantage of relatively low interest rates. Although this should reduce the amount of interest payable in the long term it did result in an additional £0.3m cost in 2015/16. The Housing Revenue Account's (HRA) contribution towards interest payable was 0.3m lower than anticipated. This was because the original capital program provided for £7.2m of HRA capital expenditure to be financed from borrowing whereas no HRA capital expenditure was actually financed from borrowing.

Interest Receivable was £0.7m more than the original estimates. This was due to the Council having more cash to invest than had been anticipated and the interest rates on the Council's investments being higher than had been anticipated.

The provision for the repayment of debt was £0.8m less than the original estimate. This is mainly because of the Councils decision to change the the method of calculating the minimum revenue provision (MRP) for the repayment of debt for post 1 April 2008 self-financed General Fund borrowing (with the exception of finance leases, service concessions and borrowing to fund long term debtors) from the equal instalment of principal method to the annuity method with effect from 2015/16 to General Fund

The ratio of Housing Revenue Account (HRA) financing costs to net revenue stream is shown below. For the HRA, this is the annual cost of financing capital expenditure, as a proportion of total gross income received including housing rents and charges.

	Original Estimate	Actual
HRA	13.4%	13.1%

The actual percentage of HRA financing costs to net revenue stream is lower than anticipated. This was because the original capital program provided for £7.2m of HRA capital expenditure to be financed from borrowing whereas no HRA capital expenditure was actually financed from borrowing.

2. ACTUAL CAPITAL EXPENDITURE 2015/16

There has been significant under spending against the original budget. Much of this was due to slippage or funding not being available. This does not represent additional capital resources. Actual capital expenditure in 2015/16 was as follows:

	Estimate £'000	**Actual £'000**
Culture & Leisure	4,355	1,360
Children's & Education Services	11,905	9,408
Environment & Community Safety	12,321	6,135
Health & Social Care (Adults Services)	5,243	407
Resources	5,798	3,550
Planning, Regeneration & Economic Development	22,759	43,995
Commercial Port	6,432	3,559
Traffic & Transportation	17,594	9,304
Housing General Fund	1,859	2,575
Local Enterprise Partnership	48,739	34,983
Total Non HRA	**137,005**	**115,276**
Housing Revenue Account (HRA)	41,720	27,437
Total	**178,725**	**142,713**

Actual capital expenditure was £36.0m below the original capital programme. The main variances were as follows:

Culture & Leisure - £3.0m Underspend

This underspend was due to slippage on the D Day Museum refurbishment and the development of the Hotwalls ARTches Studios. There were delays in obtaining funding from the Heritage Lottery Fund for the D Day Museum refurbishment. Much of the ARTches site is an ancient monument with the remainder being grade 1 listed. There were delays in consulting with Historic England and other agencies to ensure that the appropriate consents were obtained and planning conditions discharged.

Children's & Education Services - £2.5m Underspend

This underspend was due to slippage of £0.8m on the Goldsmith and Brambles Nursey expansion and £1.7m on the development of the Vanguard Centre. The Goldsmith and Brambles Nursey expansion was delayed due to finding asbestos on the site, uncertain ground conditions and contractor delays. The process of selecting a contractor for the Vanguard Centre development took longer than anticipated.

Environment and Community Safety - £6.2m Underspend

Much of this underspend is due to slippage on flood defence works. Works at Anchorage Park took longer than anticipated and the design phase of the Southsea flood works has taken longer than anticipated due to delays in obtaining approval from the Environment Agency.

Health and Social Care (Adults Services) - £4.8m Underspend

This underspend is due to the East Lodge scheme being put on hold due to the contract tender pricing being considered to be too high.

Resources - £2.2m Underspend

There was significant slippage in preparing the specifications for business intelligence, landlord's maintenance, utilities management and channel shift. In addition the residual budget for the Windows 7 upgrade was not required.

Planning, Regeneration and Economic Development - £21.2m Overspend

£32.5m was spent on acquiring commercial properties which was not included in the original budget. This was partly mitigated by an underspend of £6m on City Centre road improvements due to delays in securing funding & an underspend of £7m on the City Deal due to delays in reaching an agreement to purchase land from the private sector at Tipner West.

Commercial Port - £2.9m Underspend

The main reason for the significant underspend on the port's 2015/16 capital programme against the original estimate is because of the Floating Dock Jetty, Berth Extension and Passenger Facilities Scheme. In terms of the demolition of the Floating Dock Jetty, the contractor's original pile extraction methodology was unsuccessful which meant the scheme slipped into 2016/17. In addition, works associated with extending Berth 2 are still to commence because the feasibility study and business case identified a number of complications that still need to be resolved.

Traffic and Transportation - £8.3m Underspend

A number of capital schemes in the Traffic and Transportation Portfolio have slipped including Dunsbury Hill Farm Access Road, rebuilding the Hard Interchange, the City Centre Development Road and the Local Transport Plan. The slippage on rebuilding the Hard Interchange was particularly severe at £2.7m due to a retendering process. In addition there were a number of events within the city throughout the year which added extra pressures to the teams.

Local Enterprise Partnership (LEP) - £13.8m Underspend

The £3m Red Funnel scheme financed by the Growing Places Fund has slipped due to delays in obtaining planning permission. The £8m Solent Futures Fund has not been spent due to a significant delay in processing projects. In addition the Government has clawed back much of the uncommitted funding as part of the spending review.

Housing Revenue Account (HRA) - £14.3m Underspend

This variance is made up of two main elements: the new build programme for houses (£9.1m), and the major repairs to dwellings (£5.3m).

The building of new houses within the HRA has underspent by £9.1m, compared to the original estimate. Following the 2015 DCLG legislation on rent setting, which reduced rents for four years, the build programme had to be revised because of the reduction of available funds. This resulted in postponements and revisions of the majority of housing schemes, whilst funding sources were investigated and sought before proceeding.

The variance within the major repairs to dwellings area was mainly caused by three schemes: Hawthorn Crescent (£1m) - Works were delayed due to the lack of surveying resources; Grosvenor House (£1.6m) - Extent of the works were reviewed after 2015 new legislation introduced around rent reductions - the scheme will be on site in 2016/17, and Wilmcote House (£2.1m) - the contractor is six months behind the programme or works which has affected the cash flow and spend forecasts.

3. ACTUAL CAPITAL FINANCING REQUIREMENT

This represents the underlying requirement to borrow for capital expenditure. It takes the total value of the City Council's fixed assets and determines the amount that has yet to be repaid or provided for within the Council's accounts. The capital financing requirement also forms the basis of the calculation of the amount of money that has to be set aside for the repayment of outstanding General Fund debt. The capital financing requirement is increased each year by any new borrowing and reduced by any provision for the repayment of debt. Broadly, the higher the capital financing requirement, the higher the amount that is required to be set aside for the repayment of debt in the following year.

The actual capital financing requirements as at 31st March 2016 were as follows:

	Original Estimate	**Actual**
	£'000	£'000
Non HRA	260,185	280,516
HRA	170,166	154,734
Total	430,351	435,250

The non HRA capital financing requirement is higher than had been originally estimated due to the acquisition of commercial properties which was not included in the original budget.

The HRA capital financing requirement is lower than the original estimate due to less capital works financed by borrowing being undertaken in 2014/15 which led to a lower than anticipated opening capital financing requirement at 1 April 2015 and further underspending on capital works financed by borrowing in 2015/16.

4. ACTUAL EXTERNAL DEBT

At 31 March 2016, the City Council's level of external debt amounted to £490,378,035 consisting of the following:

- Long Term Borrowing £406,119,768
- Finance leases £2,149,010
- Service concessions (including PFI schemes) £82,109,257

The overall level of debt, excluding debt managed by Hampshire County Council, has increased between 2014/15 and 2015/16 by £27,811,939.

5. CODE OF PRACTICE

The Prudential Code requires local authorities to adopt CIPFA's Code of Practice for Treasury Management in Local Authorities. The City Council has complied with this code.

APPENDIX B

TREASURY MANAGEMENT DECISIONS 2015/16

1. GOVERNANCE

Treasury management activities were performed within the Prudential Indicators approved by the City Council.

Treasury management activities are also governed by the Treasury Management Policy Statement, Annual Minimum Revenue Provision for Debt Repayment Statement and Annual Investment Strategy approved by the City Council.

2. FINANCING OF CAPITAL PROGRAMME

The 2015/16 capital program was financed as follows:

Source of Finance	Anticipated £'000	Actual £'000
Corporate Reserves (including Capital Receipts)	19,800	5,223
Grants & Contributions	100,862	68,095
Revenue & Reserves	31,158	28,040
Long Term Borrowing	26,905	41,355
Total	178,725	142,713

There was significant slippage in the capital programme and some schemes were curtailed or abandoned. This meant that less capital resources were used to finance the capital programme.

Financing from long term borrowing is higher than had been originally estimated due to the acquisition of commercial properties which was not included in the original budget.

3. ECONOMIC BACKGROUND

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 have 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 has been 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 since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have repeatedly been revised downwards and expectations of increases in central rates have been 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, there are continuing concerns that a Greek exit has only been delayed.

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

On the international scene, concerns have 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 has also suffered disappointing growth in this financial year despite a huge programme of quantitative easing, while two of the major emerging market economies, Russia and Brazil, are in recession. The situations in Ukraine, and in the Middle East with ISIS, have also contributed to volatility.

The UK elected a majority 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 the more recent downturn in expectations for economic growth has made it more difficult to return the public sector net borrowing to a balanced annual position within the period of this parliament.

4. GROSS AND NET DEBT

The Council's net borrowing position at 31 March 2016 excluding accrued interest was as follows:

	1 April 2015	31 March 2016
	£'000	£'000
Borrowing	376,471	406,120
Finance Leases	3,027	2,149
Service Concession Arrangements (including PFIs)	83,068	82,109
Gross Debt	**462,566**	**490,378**
Investments	(321,917)	(371,827)
Net Debt	**140,649**	**118,551**

The Council has a high level of investments relative to its gross debt due to a high level of reserves, partly built up to meet future commitments under the Private Finance Initiative schemes and future capital expenditure. The £84m of borrowing taken in 2011/12 to take advantage of very low PWLB rates has also temporarily increased the Council's cash balances. The Council's investments increased by £49.9m in 2015/16. This was mainly due to borrowing £33m from them Public Works Loans Board (PWLB) in 2015/16 to fund future capital expenditure and slippage in the capital programme.

The current high level of investments increases the Council's exposure to credit risk, ie. the risk that an approved borrower defaults on the Council's investment. In the interim period where investments are high because loans have been taken in advance of need, there is also a short term risk that the rates (and therefore the cost) at which money has been borrowed will be greater than the rates at which those loans can be invested. The level of investments will fall as capital expenditure is incurred and commitments under the Private Finance Initiative (PFI) schemes are met.

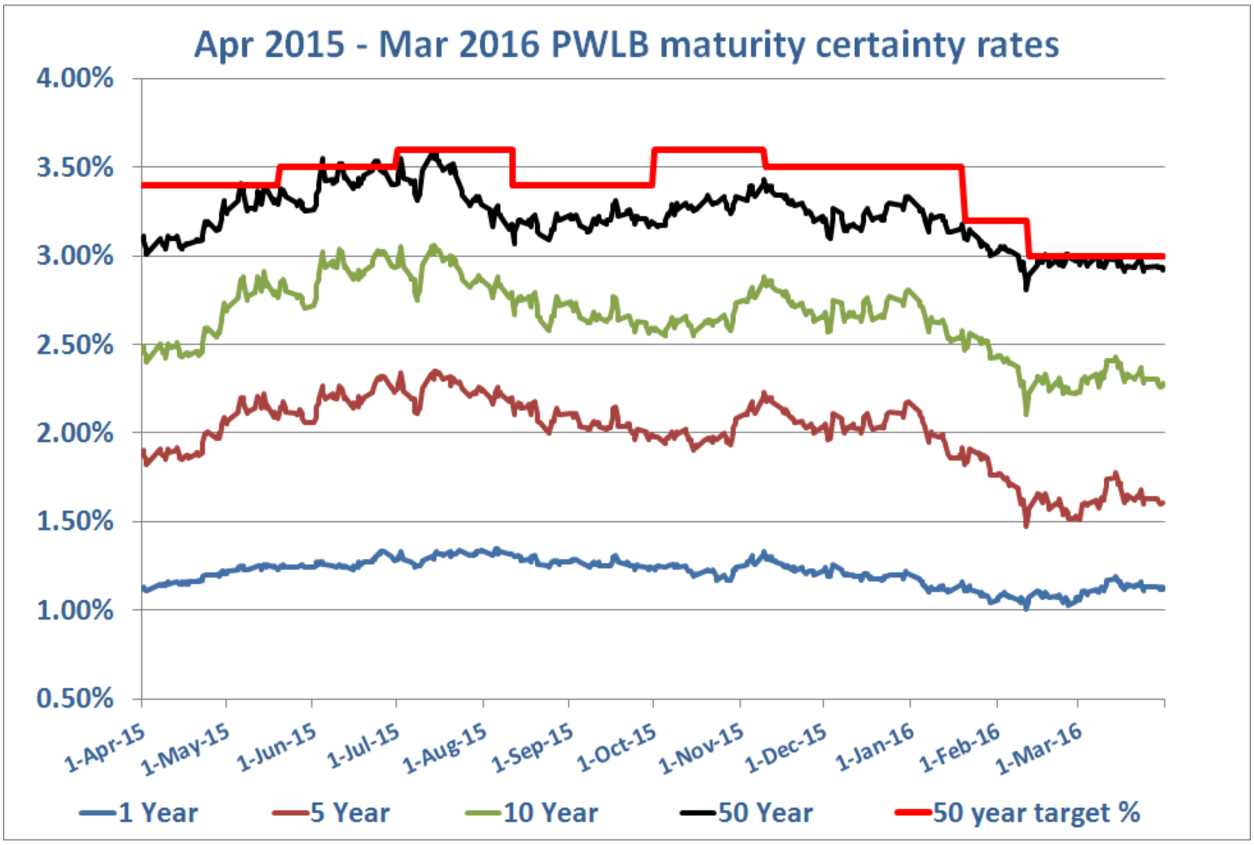
5. DEBT RESCHEDULING

Under certain circumstances it could be beneficial to use the Council's investments to repay its debt. However this normally entails paying a premium to the lender, namely the Public Works Loans Board (PWLB). Debt rescheduling is only beneficial to the revenue account when the benefits of reduced net interest payments exceed the cost of any premiums payable to the lender. Debt rescheduling opportunities have been limited in the current economic climate and by the structure of interest rates following increases in PWLB new borrowing rates in October 2010.

No debt rescheduling was undertaken in 2015/16.

6. BORROWING ACTIVITY

The table below shows the PWLB's certainty rates in 2015/16.



There were many small movements in PWLB rates in 2015/16, both upwards and downwards, but overall rates rose until June and then followed a downward trend. Any one of the movements upwards could have marked the start of an upward trend which was expected, but in the event, did not happen. PWLB rates were below the target rate recommended by the Council's advisors, Capita Asset Services, for considering new borrowing for most of the year. Consequently £9m was borrowed from the PWLB for 15 years at the project rate of 2.73% repayable at maturity in August 2015. A further £9m was borrowed from the PWLB for 15 years at the project rate which was then 2.76% repayable at maturity in December 2015. The project rate is 0.20% below the certainty rate. These loans were taken out to fund the City Deal and the development of Dunsbury Hill Farm. In February 2016 after PWLB rates had fallen the Council borrowed a further £15m for 50 years repayable at maturity at the certainty rate of 2.94% to fund future capital expenditure.

This borrowing, in addition to £88.6m borrowed at National Loans Fund Rates to fund the HRA Self Financing payment in March 2012, has resulted in the Council's external debt exceeding its capital financing requirement by £55.1m.

7. REFINANCING RISK

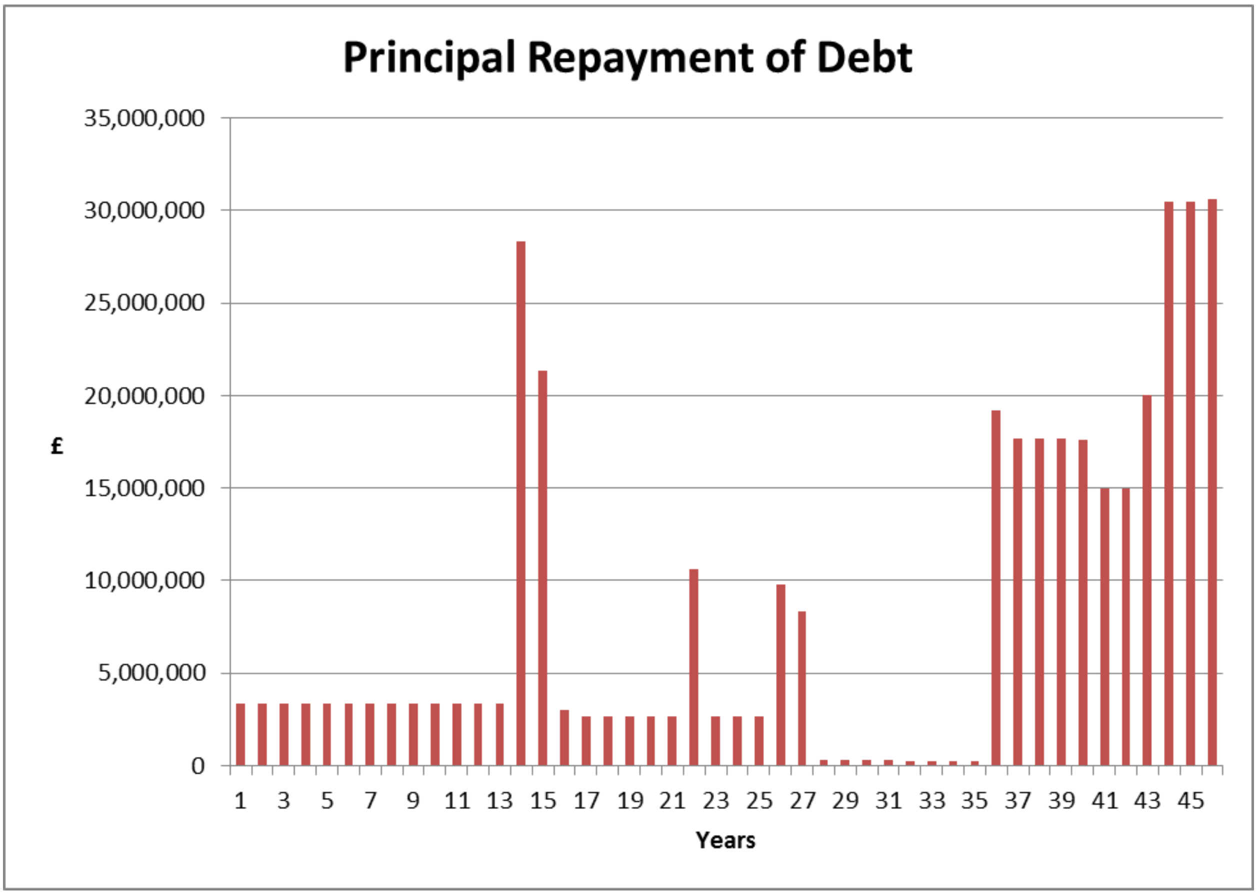
In recent years the cheapest loans have often been very long loans repayable at maturity.

During 2007/08 the Council rescheduled £70.8m of debt. This involved repaying loans from the Public Works Loans Board (PWLB) early and taking out new loans from the PWLB with longer maturities ranging from 45 to 49 years. The effect of the debt restructuring was to reduce the annual interest payable on the Council’s debt and to lengthen the maturity profile of the Council’s debt.

£50m of new borrowing was taken in 2008/09 to finance capital expenditure. Funds were borrowed from the PWLB at fixed rates of between 4.45% and 4.60% for between 43 and 50 years.

A further £173m was borrowed in 2011/12 to finance capital expenditure and the HRA Self Financing payment to the Government. Funds were borrowed from the PWLB at rates of between 3.48% and 5.01%. £89m of this borrowing is repayable at maturity in excess of 45 years. The remaining £84m is repayable in equal instalments of principal over periods of between 16 and 26 years.

As a result of interest rates in 2007/08 when the City Council rescheduled much of its debt and interest rates in 2008/09 and 2011/12 when the City Council undertook considerable new borrowing 64% of the City Council’s debt matures in over 30 years' time.



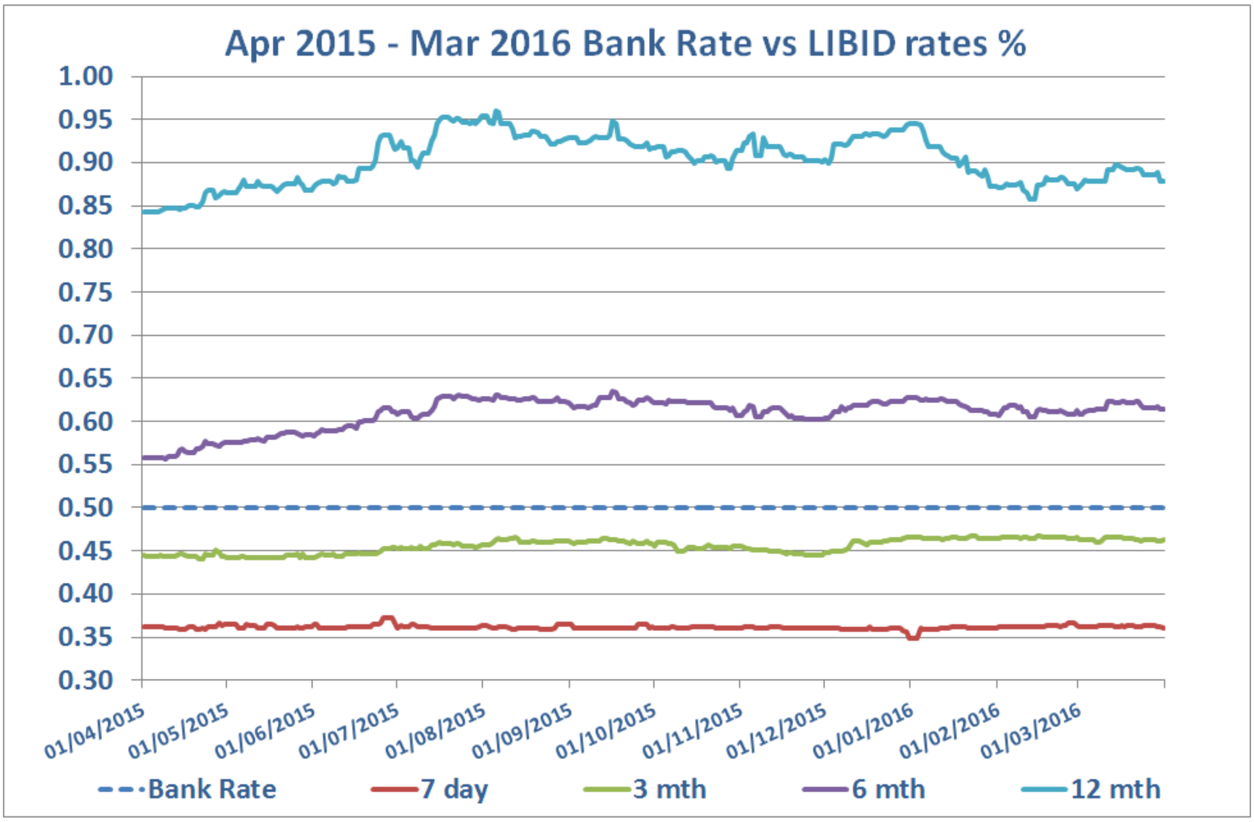
The CIPFA Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes require local authorities to set upper and lower limits for the maturity of borrowings in defined periods. The Council's performance against the limits set by the City Council is shown below.

	Under 1 Year	**1 to 2 Years**	**3 to 5 Years**	**6 to 10 Years**	**11 to 20 Years**	**21 to 30 Years**	**31 to 40 Years**	**41 to 50 Years**
Lower Limit	0%	0%	0%	0%	0%	0%	0%	0%
Upper Limit	10%	10%	20%	20%	40%	40%	40%	50%
Actual	1%	1%	2%	4%	18%	10%	22%	42%

8. INVESTMENT ACTIVITY

Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained 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.

London inter-bank lending rates in 2015/16 are shown in the graph below:



The average return on the Council's investments was 0.97% in 2015/16 which was an improvement to the average return of 0.76% in 2014/15. This was achieved through lengthening the average duration of the portfolio (longer investments generally offer better returns) and reducing the amount invested in local authorities which offer very secure investments but low returns.

The City Council's investment activities are benchmarked by Capita Asset Services against its other clients. The graph below shows the councils' weighted average rates of return (WARoR) as at 31 March 2016 compared to a model WARoR taking account of duration risk and credit risk. The returns on Portsmouth's investment portfolio are in line with where they should be given the risks inherent in the portfolio.

	Actual WARoR	Model WARoR	Difference	Lower Bound	Upper Bound	Performance
Portsmouth City Council	1.11%	1.05%	0.05%	1.00%	1.11%	Inline

Portsmouth is slightly above the model band width indicating that Portsmouth's returns are a little better than would be expected for the degree of credit and duration risk inherent in the portfolio.

9. SECURITY OF INVESTMENTS

The risk of default has been managed through limiting investments in any institution to a maximum £30m, setting investment limits for individual institutions that reflect their financial strength and spreading investments over countries and sectors.

The 2015/16 Treasury Management Policy approved by the City Council on 17 March 2015 and amended by the City Council on 10 November only permitted deposits to be placed with the Council's subsidiaries, namely MMD (Shipping Services) Ltd, the United Kingdom Government, other local authorities and institutions that have the following minimum credit ratings:

<u>Short Term Rating</u>

F2 (or equivalent) from Fitch, Moody's (P-2) or Standard and Poor (A-2)

<u>Long Term Rating</u>

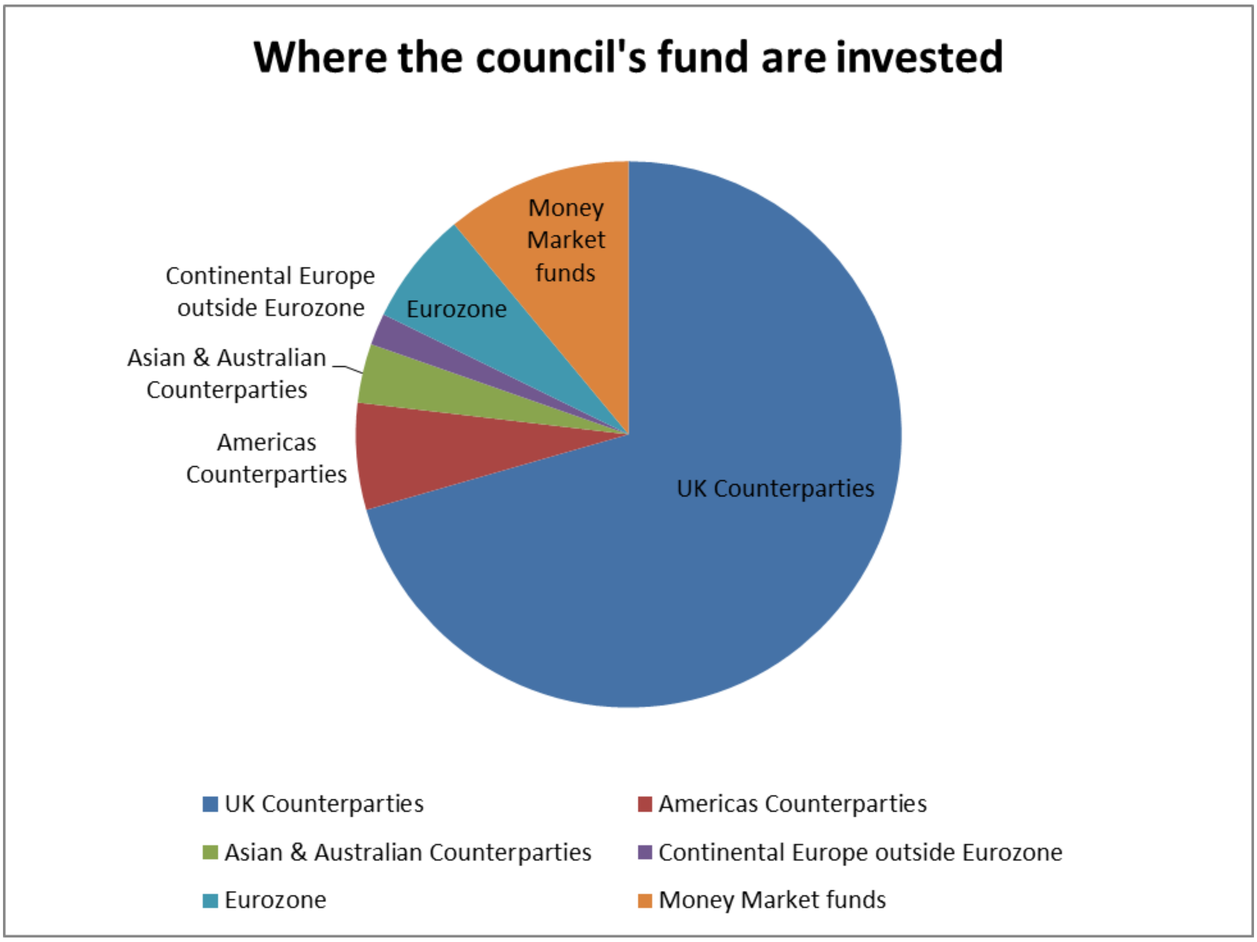
BBB

In addition the 2015/16 Treasury Management Policy approved by the City Council on 17 March 2015 also permitted deposits to be placed with the stronger unrated building societies.

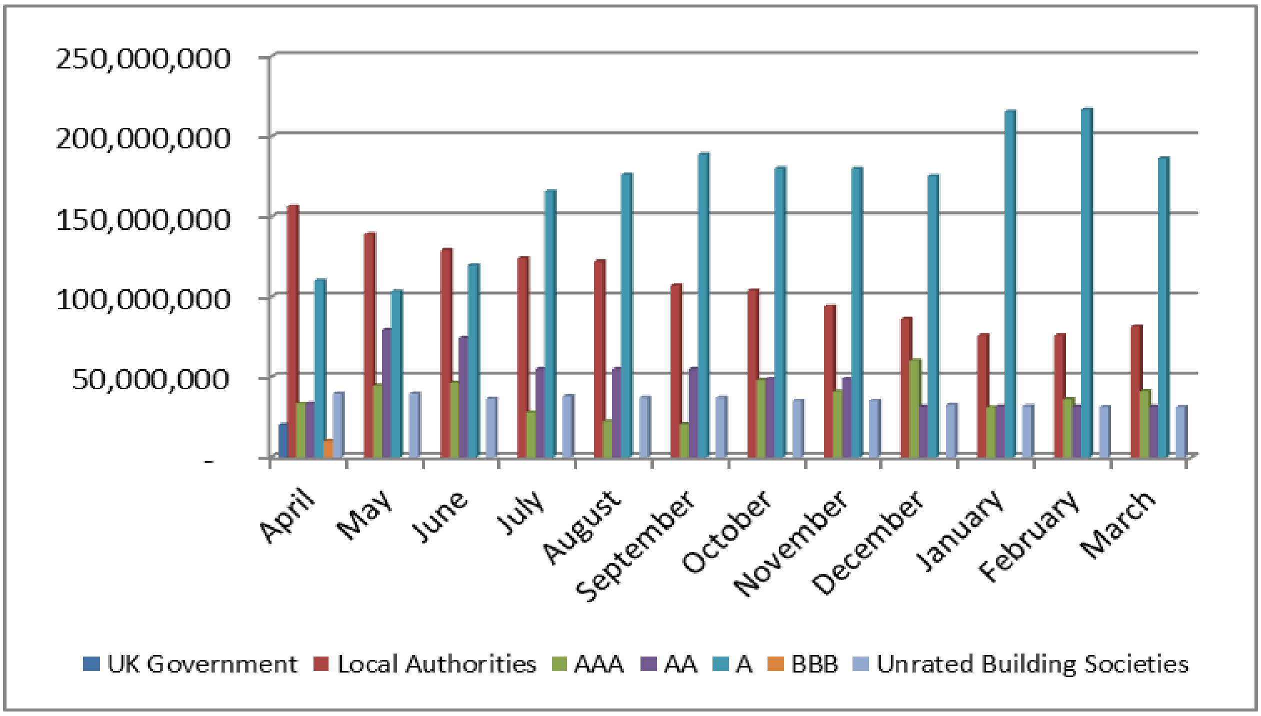
At 31 March 2016 the City Council had on average £6.8m invested with each institution.

Credit risk also exists from the Council's current bank accounts. This arises not only from the Council's overnight current account bank balances, but also from settlement risk, ie. the Council's intra-day exposure can temporarily exceed the balance on the accounts after all transactions have been processed. This counter party exposure is in addition to the Council's investment limits.

The chart below shows how the Council’s funds were invested at 31 March 2016.



The chart below shows how the Council's investment portfolio has changed in terms of the credit ratings of investment counter parties over 2015/16.

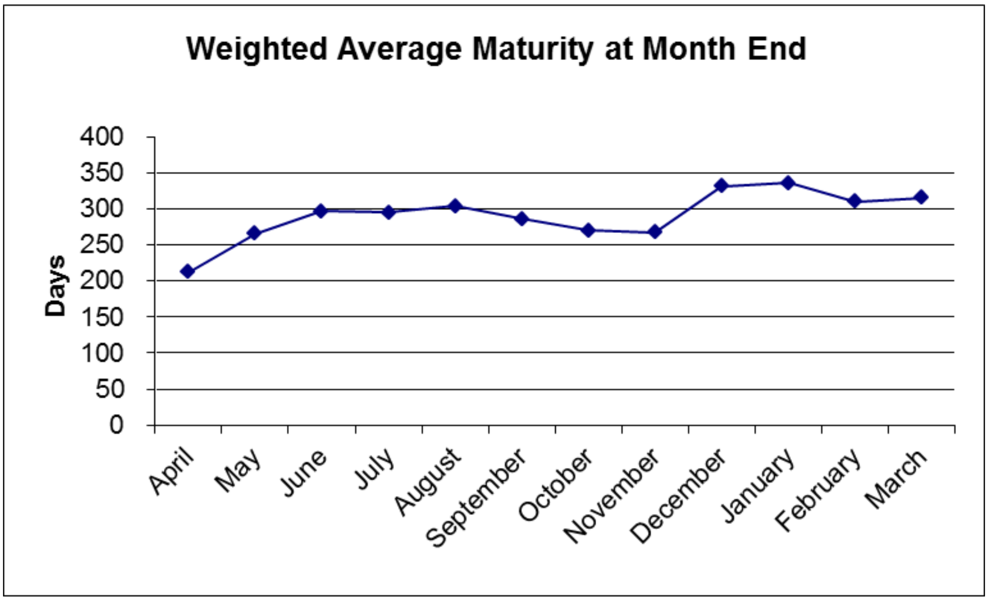


It can be seen from the graph above that investments in local authorities have declined over 2015/16. These investments have largely been replaced by investments in A rated private sector counter parties which generally offer a better return than investments in local authorities.

10. LIQUIDITY OF INVESTMENTS

The 2015/16 Treasury Management Policy seeks to maintain the liquidity of the portfolio, ie. the ability to liquidate investments to meet the Council's cash requirements, through maintaining at least £10m in instant access accounts. At 31 March 2016 £41.6m was invested in instant access accounts. Whilst short term investments provide liquidity and reduce the risk of default, they do also leave the Council exposed to falling interest rates.

The weighted average maturity of the City Council’s investment portfolio started at 212 days in April and rose to 315 days in March. Investment rates are expected to fall further and the longer maturity pattern of the investment portfolio will delay the effect that this will have in diminishing the returns on the Council's investments. This is shown in the graph below.



Under CIPFA’s Treasury Management Code it is necessary to specify limits on the amount of long term investments, ie. Investments exceeding 364 days that have maturities beyond year end in order to ensure that sufficient money can be called back to meet the Council’s cash flow requirements. The Council’s performance against the limits set by the City Council is shown below.

	Limit **(Not Exceeding)** £m	**Actual** £m
31/3/2016	243	196
31/3/2017	231	106
31/3/2018	228	33

11. INTEREST RATE RISK

This is the risk that interest rates will move in a way that is adverse to the City Council's position.

The CIPFA Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes require local authorities to set upper limits for fixed interest rate exposures. Fixed interest rate borrowing exposes the Council to the risk that interest rates could fall and the Council will pay more interest than it need have done. Long term fixed interest rate investments expose the Council to the risk that interest rates could rise and the Council will receive less income than it could have received. However fixed interest rate exposures do avoid the risk of budget variances caused by interest rate movements. The Council's performance against the limit set by the City Council as at 31 March 2016 is shown below.

	Limit **£m**	**Actual** **£m**
Maximum Projected Gross Borrowing – Fixed Rate	395	406
Minimum Projected Gross Investments – Fixed Rate	(91)	(186)
Fixed Interest Rate Exposure	304	220

Although the Council ended the year with more fixed rate gross borrowing than had been allowed for it also had a far greater level of long term fixed rate investments than had been anticipated leaving the Council well within its fixed interest rate exposure limit.

The CIPFA Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes also require local authorities to set upper limits for variable interest rate exposures. Variable interest rate borrowing exposes the Council to the risk that interest rates could rise and the Council's interest payments will increase. Short term variable interest rate investments expose the Council to the risk that interest rates could fall and the Council's investment income will fall. Variable interest rate exposures carry the risk of budget variances caused by interest rate movements. The Council's performance against the limit set by the City Council is shown below.

	Limit £m	Actual £m
Minimum Projected Gross Borrowing – Variable Rate	-	-
Maximum Projected Gross Investments – Variable Rate	(278)	(186)
Variable Interest Rate Exposure	(278)	(186)

12. REVENUE COSTS OF TREASURY MANAGEMENT ACTIVITIES IN 2015/16

Expenditure on treasury management activities against the revised budget is shown below.

Interest 2015/16

	Revised Estimate 2015/16 £000	Actual 2015/16 £000	Variance +/- £000
PWLB – Maturity Loans	11,595	11,635	40
PWLB - E.I.P Loans	3,699	3,697	(2)
Other Long Term Loans	512	516	4
HCC Transferred Debt	439	442	3
Interest on Finance Lease	302	302	-
Interest on Service Concession Arrangements (including PFIs)	8,920	8,901	(19)
Interest Payable to External Organisations	16	1	(15)
	25,483	25,494	11
Deduct			
Investment Income	(4,670)	(5,318)	(648)
	20,813	20,176	(637)
Provision for Repayment of Debt	9,259	9,206	(53)
Debt Management Costs	465	398	(67)
	30,537	**29,780**	**(757)**

Net treasury management costs were £0.8m below the revised budget mainly due to investment returns being higher than had been anticipated.