Title of Meeting	Cabinet City Council
Subject:	Treasury Management Mid-Year Review for 2015/16
Date of decision:	5 November 2015 (Cabinet) 6 November 2015 (Governance, Audit & Standards Committee – Information only) 10 November 2015 (City Council)
Report by:	Chris Ward, Director of Financial & Information Services and Section 151 Officer
Wards affected:	All

Key decision: Yes
Budget & policy framework decision: Yes

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1. Purpose of report

The purpose of the report is to review the current treasury management position and strategy and make recommendations to improve the strength and performance of the treasury management operation. This report seeks to amend the minimum revenue provision (MRP) policy for the repayment of unsupported borrowing, to allow a wider range of investments to be made on the basis of a single credit rating, and to review the investment counter party limits. Appendix A aims to inform members and the wider community of the Council's Treasury Management position at 30 September 2015 and of the risks attached to that position.

2. Recommendations

1. That the annuity method of calculating the minimum revenue provision (MRP) for the repayment of debt is applied with effect from 2015/16 to General Fund post 1 April 2008 self-financed borrowing excluding:

    - Finance Leases
    - Service concessions (including Private Finance Initiative schemes)
    - Borrowing to fund long term debtors (including finance leases);

2. That investments be made in enhanced or cash plus money market funds on the basis of a single credit rating and that these be treated as category 6 investments

3. That the investment counter party limits be revised as shown in Appendix B

4. That the following investment duration limits be approved:

	Maximum Duration Limit
Category 1 United Kingdom Government including the Debt Management Office Deposit Facility	Up to 5 years
Category 2 Local authorities in England, Scotland and Wales	Up to 5 years
Category 3 RSLs with a single long term credit rating of Aa-	Up to 10 years
Category 4 Banks (including equity trackers) with a short term credit rating of F1+ and a long term rating of Aa-. Aaa rated money market funds.	Up to 5 years
Category 5 RSLs with a single A long term credit rating of A-	Up 10 years
Category 6 Banks (including equity trackers) and corporate bonds with a short term credit rating of F1 and a long term rating of A+. Building societies with a short term credit rating of F1 and a long term rating of A. Enhanced money market funds with a single AA credit rating.	Up to 5 years.
Category 7 Banks (including equity trackers) and corporate bonds with a short term credit rating of F1 and a long term rating of A. Building societies with a short term credit rating of F1 and a long term rating of A-.	Up to 5 years
Category 8 Banks (including equity trackers) and corporate bonds with a short term credit rating of F1 and a long term rating of A-.	Up to 5 years
Category 9 Building societies with a short term credit rating of F2 and a long term rating of BBB.	Up to 2 years
Category 10 Unrated building societies in the strongest financial position	Up to 2 years
Category 11 Unrated building societies in a strong financial position	Up to 364 days

5. That the following actual Treasury Management indicators for the second quarter of 2015/16 be noted:

(a) The Council's debt at 30 September was as follows:

Prudential Indicator 2015/16	**Limit** £M	**Position at 30/9/15** £M
Authorised Limit	503	469
Operational Boundary	484	469

(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**
Lower Limit	0%	0%	0%	0%	0%	0%	0%	0%
Upper Limit	20%	20%	30%	30%	40%	40%	60%	70%
Actual	1%	4%	3%	4%	17%	11%	19%	41%

(c) The Council's interest rate exposures at 30 September 2015 were:

	Limit £m	**Actual** £m
Fixed Interest	304	218
Variable Interest	(358)	(242)

(d) Sums invested for periods longer than 364 days at 30 September 2015 were:

Maturing after	Original Limit £m	Actual £m
31/3/2016	243	159
31/3/2017	231	70
31/3/2018	228	5

3. Background

CIPFA's Treasury Management Code requires a Treasury Management Mid-Year Review to be considered by the City Council. The Council's treasury management position at 30 September and the risks attached to that position are reported in Appendix A.

The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 require each authority to "determine for the current financial year an amount of minimum provision which it considers prudent". Our current policy uses the asset life equal instalment method. However, 60% of the Council's borrowings mature in over 30 years meaning that funds are set aside in advance of need. All but £11m of the Council's borrowing is PWLB debt. The PWLB introduced new lower discount rates to calculate premiums on the early repayment of debt in 2010. The increased premiums resulting from this means that the existing debt is unlikely to be repaid early or rescheduled. In the meantime providing MRP using the asset life equal instalment method is contributing to the Council's high cash balances. The need to invest such high cash balances exposes the Council to credit risk in the event that one of the Council's investment counterparties gets into financial difficulties.

The Council has to hold some of its cash in liquid investments in order to meet its expenditure obligations when they fall due. The Council currently invests its short term cash in instant access money market funds which are currently yielding around 0.46%.

The Council changed its provider for investment counter party information on 1st May following the expiry of the previous contract. In addition there have been some changes to the credit ratings of the Council's investment counterparties.

The Council's investment strategy approved by the City Council on 17 March 2015 set various duration limits for different investments depending on their credit quality.

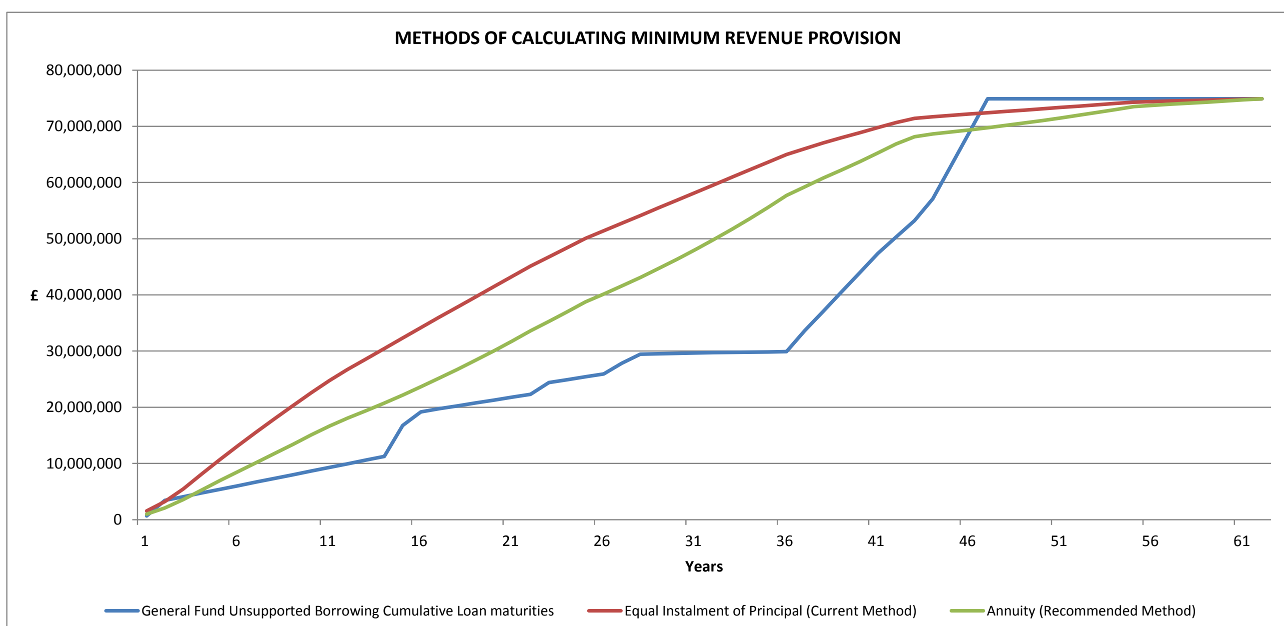
Portsmouth CITY COUNCIL

4. Reasons for Recommendations

It is recommended that the annuity method of calculating minimum revenue provision (MRP) for the repayment of debt is applied with effect from 2015/16 to General Fund post 1 April 2008 self-financed borrowing excluding:

- Finance Leases
- Service concessions (including Private Finance Initiative schemes)
- Borrowing to fund long term debtors (including finance leases)

This will still ensure that provision is made for the repayment of unsupported borrowing within the life of the assets that it is used to finance, but in a way that better reflects the maturity pattern of the Council's borrowing and avoids the credit risk associated with providing for the repayment of debt long before there is any realistic chance of the debt actually being repaid. The graph below illustrates this point.



It should also be borne in mind that the real value of the Council's long term borrowing will be considerably eroded by inflation prior to it becoming due for repayment which is a further argument for not providing for its repayment excessively early.

Separate arrangements exist to provide MRP for finance leases, service concessions and borrowing to fund long term debtors. MRP on finance leases and service concessions including Private Finance Initiative (PFI) arrangements equals the charge that goes to write down the balance sheet liability. The principal element of the income receivable from long term debtors is set aside to repay debt if the asset was financed through self-financed borrowing in order that the repayment of the debt is financed from the capital receipt. The principal element of the rent receivable from finance leases is set aside to repay debt if the asset was financed through self-financed borrowing in order that the repayment of the debt is financed from the capital receipt. It is not recommended that these arrangements be changed.

The returns on the Council's short term cash could be significantly enhanced by investing funds where same day access is not required in enhanced or cash plus money market funds which require two to four days' notice of withdrawals. These funds only have a single credit rating whereas the Council's investment policy generally requires investment counter parties to have two credit ratings. This provides the Council with greater assurance as it is relying on the analysis of two credit rating agencies rather than just one. However there is a cost to obtaining multiple credit ratings and enhanced or cash plus funds only have a single credit rating. It is therefore recommended that investments be made in enhanced or cash plus money market funds on the basis of a single credit rating. These funds have AA or AAA credit ratings. However it is recommended that these funds be treated as category 6 (A+) investments to reflect the increased risk of relying on a single credit rating (as opposed to category 4 if two ratings had been obtained).

The Council's new supplier of counter party information has suggested some additional counter parties that meet the Council's credit criteria. It is recommended that these be added to the Council's investment counter party list and that the investment limits be revised to take account of any changes to counter party's credit ratings.

Following the City Council's decision on 13 October to permit unsecured investments with a duration in excess of 2 years to be placed with banks; it is recommended that the following investment duration limits in the investment strategy be approved:

	Maximum Duration Limit
Category 1 United Kingdom Government including the Debt Management Office Deposit Facility	Up to 5 years
Category 2 Local authorities in England, Scotland and Wales	Up to 5 years
Category 3 RSLs with a single long term credit rating of Aa-	Up to 10 years
Category 4 Banks (including equity trackers) with a short term credit rating of F1+ and a long term rating of Aa-. Aaa rated money market funds.	Up to 5 years
Category 5 RSLs with a single A long term credit rating of A-	Up 10 years
Category 6 Banks (including equity trackers) and corporate bonds with a short term credit rating of F1 and a long term rating of A+. Building societies with a short term credit rating of F1 and a long term rating of A. Enhanced money market funds with a single credit rating of AA.	Up to 5 years.
Category 7 Banks (including equity trackers) and corporate bonds with a short term credit rating of F1 and a long term rating of A. Building societies with a short term credit rating of F1 and a long term rating of A-.	Up to 5 years
Category 8 Banks (including equity trackers) and corporate bonds with a short term credit rating of F1 and a long term rating of A-.	Up to 5 years
Category 9 Building societies with a short term credit rating of F2 and a long term rating of BBB.	Up to 2 years
Category 10 Unrated building societies in the strongest financial position	Up to 2 years
Category 11 Unrated building societies in a strong financial position	Up to 364 days

5. Equality impact assessment (EIA)

The contents of this report do not have any relevant equalities impact and therefore an equalities impact assessment is not required.

6. 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.

7. Director of Finance's comments

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

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Signed by Director of Financial Services & IS (Section 151 Officer)

Appendices:
Appendix A: Treasury Management Mid-Year Review 2015/16
Appendix B: Investment Counter Party List

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 Treasury Management Files	Financial Services
2	

The recommendation(s) set out above were approved/ approved as amended/ deferred/ rejected by the City Council on 10 November 2015.

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

APPENDIX A

TREASURY MANAGEMENT MID YEAR REVIEW OF 2015/16

1. GOVERNANCE

The Treasury Management Policy Statement, Annual Minimum Revenue Provision for Debt Repayment Statement and Annual Investment Strategy approved by the City Council on 17 March 2015 provide the framework within which Treasury Management activities are undertaken.

2. ECONOMIC UPDATE

United Kingdom

UK gross domestic product (GDP) growth rates in 2013 of 2.2% and 2.9% in 2014 were the strongest growth rates of any G7 country; the 2014 growth rate was also the strongest UK rate since 2006 and the 2015 growth rate is likely to be a leading rate in the G7 again, possibly being equal to that of the US. However, quarter 1 of 2015 was weak at +0.4% (+2.9% y/y) though there was a rebound in quarter 2 to +0.7% (+2.4% y/y). Growth is expected to weaken marginally to about +0.5% in quarter 3 as the economy faces headwinds for exporters from the appreciation of Sterling against the Euro and weak growth in the EU, China and emerging markets, plus the dampening effect of the Government's continuing austerity programme, although the pace of reductions was eased in the May Budget.

Despite these headwinds, the Bank of England is forecasting growth to remain around 2.4 – 2.8% over the next three years, driven mainly by strong consumer demand as the squeeze on the disposable incomes of consumers has been reversed by a recovery in wage inflation at the same time that CPI inflation has fallen to, or near to, zero over the last quarter. Investment expenditure is also expected to support growth.

The August Bank of England Inflation Report forecast was notably subdued with inflation barely getting back up to the 2% target within the 2-3 year time horizon. However, with the price of oil taking a fresh downward direction and Iran expected to soon re-join the world oil market after the impending lifting of sanctions, there could be several more months of low inflation still to come, especially as world commodity prices have generally been depressed by the Chinese economic downturn.

There are therefore considerable risks around whether inflation will rise in the near future as strongly as previously expected; this will make it more difficult for the central banks of both the US and the UK to raise rates as soon as had previously been expected, especially given the recent major concerns around the slowdown in Chinese growth, the knock on impact on the earnings of emerging countries from falling oil and commodity prices, and the volatility we have seen in equity and bond markets in 2015 so far, which could potentially spill over to impact the real economies rather than just financial markets.

United States

The American economy has made a strong comeback after a weak first quarter's growth at +0.6% (annualised), to grow by no less than 3.9% in quarter 2 of 2015. While there had been confident expectations during the summer that the Fed. could start increasing rates at its meeting on 17 September, or if not by the end of 2015, the recent downbeat news about Chinese and Japanese growth and the knock on impact on emerging countries that are major suppliers of commodities, was cited as the main reason for the Fed's decision to pull back from making that start. This has led to a reappraisal of the likelihood of any increase occurring in 2015 with early 2016 now being widely regarded as being more likely.

Eurozone (EZ)

In the Eurozone, the European Central Bank (ECB) fired its big bazooka in January 2015 in unleashing a massive €1.1 trillion programme of quantitative easing to buy up high credit quality government and other debt of selected EZ countries. This programme of €60bn of monthly purchases started in March 2015 and it is intended to run initially to September 2016. This already appears to have had a positive effect in helping a recovery in consumer and business confidence and a start to a significant improvement in economic growth. GDP growth rose to 0.5% in quarter 1 2015 (1.0% y/y) but came in at +0.4% (+1.5% y/y) in quarter 2 and looks as if it may maintain this pace in quarter 3. However, the recent downbeat Chinese and Japanese news has raised questions as to whether the ECB will need to boost its QE programme if it is to succeed in significantly improving growth in the EZ and getting inflation up from the current level of around zero to its target of 2%.

3. INTEREST RATE FORECAST

The Council's treasury advisor, Capita Asset Services, has provided the following forecast:

	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18
Bank rate	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.50%	1.50%	1.75%	1.75%
5yr PWLB rate	2.40%	2.50%	2.60%	2.80%	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%
10yr PWLB rate	3.00%	3.20%	3.30%	3.40%	3.50%	3.70%	3.80%	3.90%	4.00%	4.10%	4.20%
25yr PWLB rate	3.60%	3.80%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.60%	4.60%
50yr PWLB rate	3.60%	3.80%	3.90%	4.00%	4.10%	4.20%	4.30%	4.40%	4.50%	4.60%	4.60%

Capita Asset Services undertook a review of its interest rate forecasts on 11 August. Later in August, fears around the slowdown in China and Japan caused major volatility in equities and bonds and sparked a flight from equities into safe havens like gilts and so caused PWLB rates to fall. However, there is much volatility in rates as news ebbs and flows in negative or positive ways and news in September in respect of Volkswagen, and other corporates, has compounded downward pressure on equity prices. This latest forecast includes a first increase in Bank Rate in quarter 2 of 2016.

Despite market turbulence in late August, and then September, causing a sharp downturn in PWLB rates, the overall trend in the longer term will be for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK, and of bond issuance in other major western countries. Increasing investor confidence in eventual world economic recovery is also likely to compound this effect as recovery will encourage investors to switch from bonds to equities.

The overall balance of risks to economic recovery in the UK is currently evenly balanced. Only time will tell just how long this current period of strong economic growth will last; it also remains exposed to vulnerabilities in a number of key areas.

Downside risks to current forecasts for UK gilt yields and PWLB rates currently include:

- Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.
- UK economic growth turns significantly weaker than we currently anticipate.
- Weak growth or recession in the UK's main trading partners - the EU, US and China.

- A resurgence of the Eurozone sovereign debt crisis.
- Recapitalisation of European banks requiring more government financial support.
- Monetary policy action failing to stimulate sustainable growth and to combat the threat of deflation in western economies, especially the Eurozone and Japan.
- Emerging country economies, currencies and corporates destabilised by falling commodity prices and / or the start of United States Fed. rate increases, causing a flight to safe havens

The potential for upside risks to current forecasts for UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- Uncertainty around the risk of a UK exit from the EU.
- The ECB severely disappointing financial markets with a programme of asset purchases which proves insufficient to significantly stimulate growth in the EZ.
- The commencement by the US Federal Reserve of increases in the Fed. funds rate in 2015, causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.
- UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

4. NET DEBT

The Council's net borrowing position excluding accrued interest at 30 September 2015 was as follows:

	1 April 2015	30 September 2015
	£'000	£'000
Borrowing	376,471	383,795
Finance Leases	3,027	2,740
Service Concession Arrangements (including Private Finance Initiative)	83,068	82,589
Gross Debt	**462,566**	**469,124**
Investments	(321,917)	(408,236)
Net Debt	**140,649**	**60,888**

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. However these reserves are fully committed and are not available to fund new expenditure. The £84m of borrowing taken in 2011/12 to take advantage of the very low PWLB rates has also temporarily increased the Council's cash balances.

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

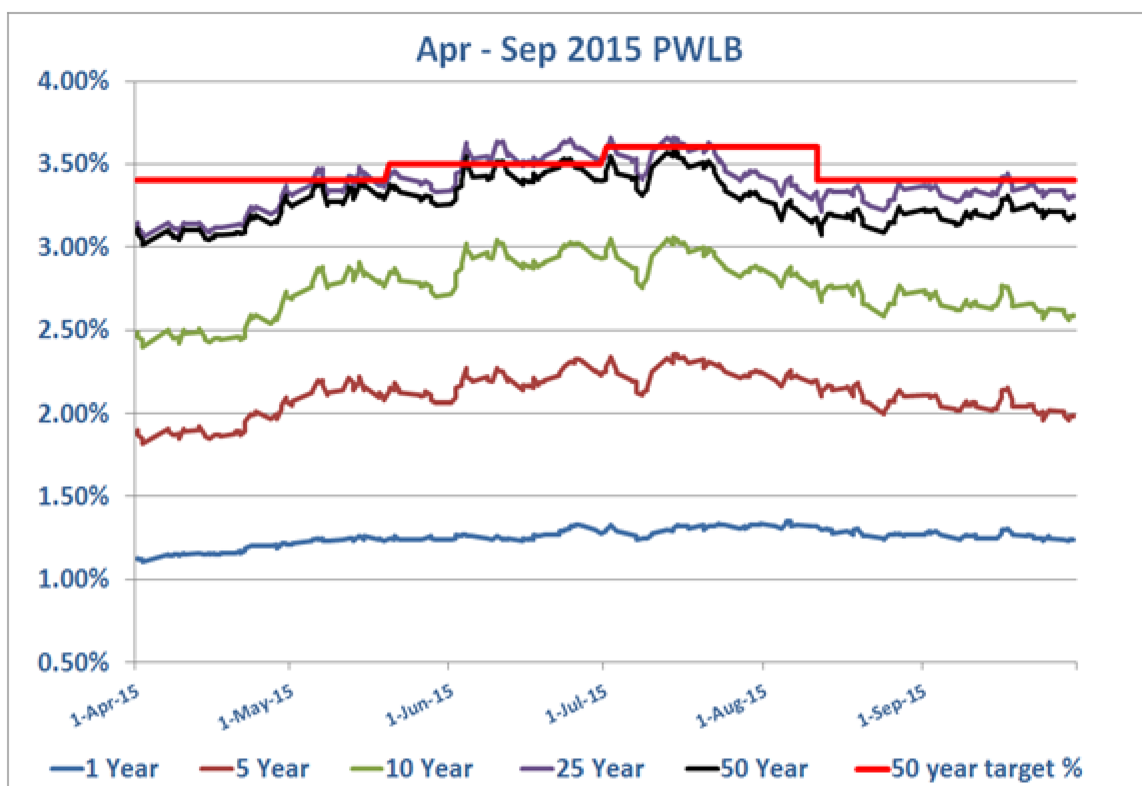
Under certain circumstances it could be beneficial to use the Council's investments to repay its debt. However this normally entails paying a premium to the lender, namely the Public Works Loans Board (PWLB). Debt rescheduling is only beneficial to the revenue account when the benefits of reduced net 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 during the first half of the year.

6. BORROWING ACTIVITY

The City Council has access to borrow £18m from the Public Works Loans Board (PWLB) at the project rate in 2015/16 to fund the development of Tipner, Horsea Island and Dunsbury Hill Farm. The project rate is 0.2% less than the certainty rate that the PWLB normally offers to the Council.

The graph below shows the PWLB's certainty rates in the first six months of 2015/16.



There were many small movements in PWLB rates in the first six months of 2015/16, both upwards and downwards, but overall the general trend has been an increase in interest rates during the first quarter but then a fall during the second quarter. There was a dip in PWLB rates on 24th August and £9m was borrowed from the PWLB at the project rate which was 2.73% at the time. The loan has a term of 15 years repayable at maturity in August 2030.

The remaining £9m of the allocation will be borrowed at a time when PWLB rates are favourable.

The Council's debt at 30 September was as follows:

Prudential Indicator 2015/16	Limit £M	Position at 30/9/14 £M
Authorised Limit	503	469
Operational Boundary	484	469

7. MATURITY STRUCTURE OF BORROWING

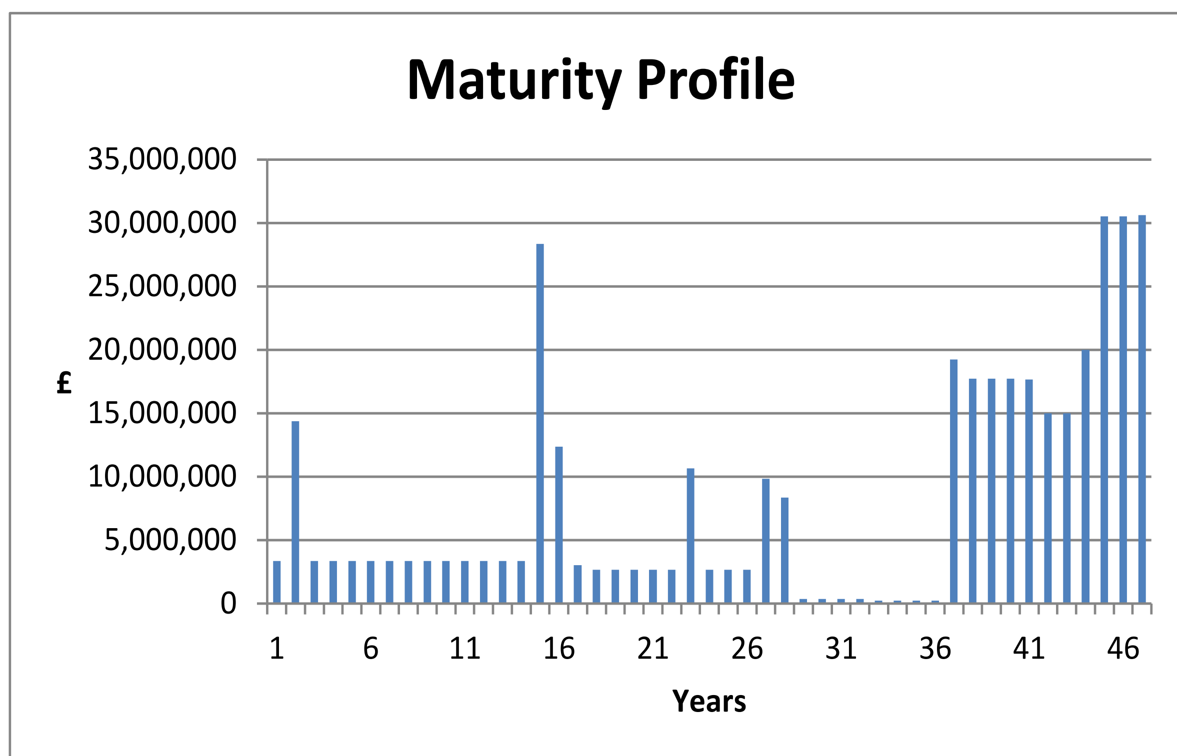
In recent years the cheapest loans have often been very long loans repayable at maturity.

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 48 years. The remaining £84m is repayable in equal installments of principal over periods of between 20 and 31 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 60% of the City Council's debt matures in over 30 years' time. This is illustrated in graph below.



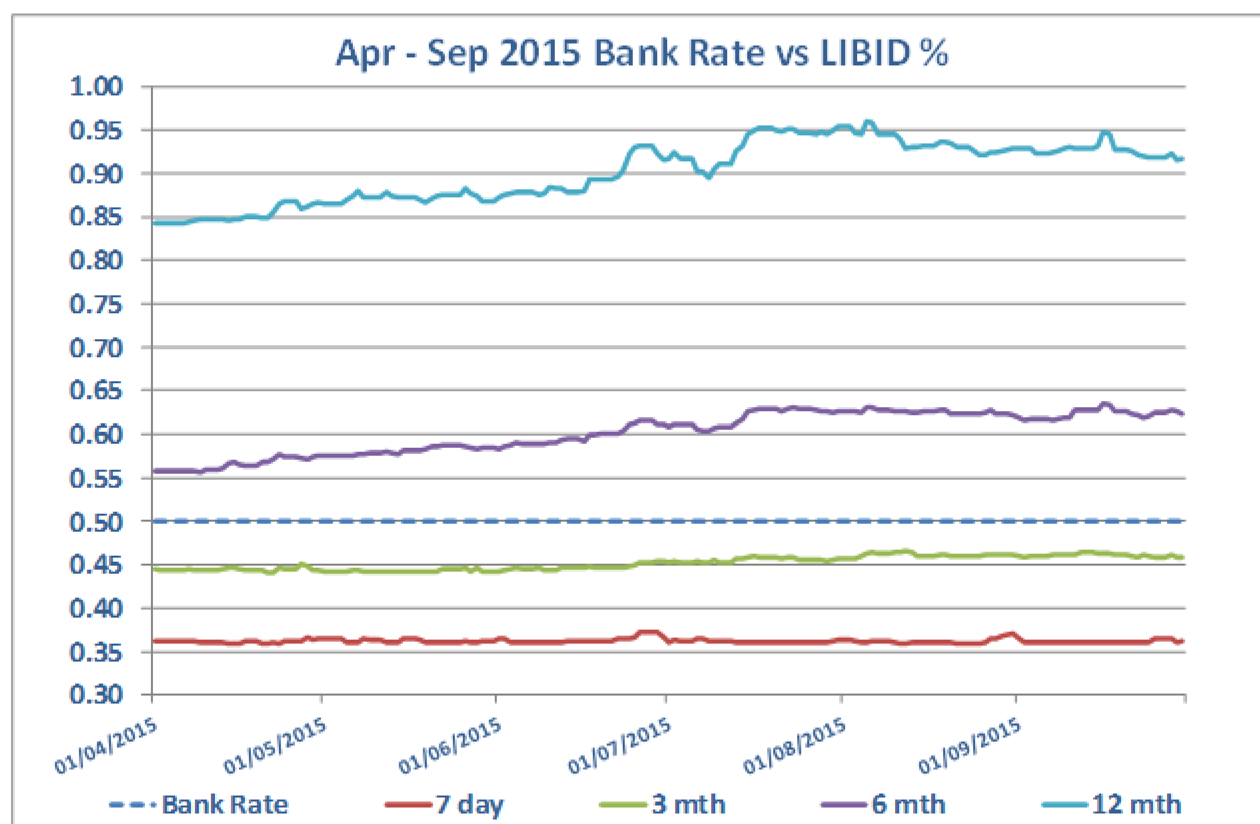
CIPFA's Treasury Management in the Public Services Code of Practice which the City Council is legally obliged to have regard to requires local authorities to set upper and lower limits for the maturity structure of their borrowing. The limits set by the City Council on 17 March together with the City Councils actual debt maturity pattern are 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	20%	20%	30%	30%	40%	40%	60%	70%
Actual	1%	4%	3%	4%	17%	11%	19%	41%

8. INVESTMENT ACTIVITY

In accordance with the Government's statutory guidance, it is the Council's priority to ensure security of capital and liquidity, and to obtain an appropriate level of return which is consistent with the Council's risk appetite. It is a very difficult investment market in terms of earning the level of interest rates commonly seen in previous decades as rates are very low and in line with the 0.5% Bank Rate.

Short term market interest rates for the first half of 2015/16 are shown in the graph below:



The Council's investment portfolio has increased by £86.3m from £321.9m to £408.2m. This resulted in up to £85m being invested in AAA rated money market funds and 1 month UK Government Treasury Bills which paid interest of between 0.33 and 0.42% until it was possible to invest these funds for a longer term at higher interest rates. This caused the average return on the Council's investments to fall from 0.76% in 2014/15 to 0.68% in the first quarter of 2015/16. Despite this the Council has been able to reduce its investments in other local authorities by £54.5m from £161.5m to £107.0m. Local authorities are currently typically offering 0.5% for a year or 0.9% for two years compared to 1.05% for a year or 1.25% for two years from other borrowers.

The overall investment portfolio yield for the first six months of the year is 0.76%.

The Council's budgeted investment return for 2015/16 is £2,297k, and performance for the year to date is £376k above budget. This is due to having more cash to, invest than had been anticipated and improved investment returns.

9. REVSION OF INVESTMENT COUNTER PARTIES

The Council changed its provider for counter party information on 1st May following the expiry of the previous contract. The Council's new supplier of counter party information has suggested some additional counter parties that meet the Council's credit criteria.

In addition there have been a lot of changes to institutions credit ratings in the first six months of 2015/16. Following the financial crisis many governments, including the UK government, put bank resolution arrangements in place so that if a bank fails in future, it will be depositors that fund the resolution of the failure rather than the tax payer. This resulted in numerous banks being placed on negative outlook by the credit rating agencies as they considered whether uplifts to credit ratings on the basis of sovereign support were still justified. At the same time the regulatory authorities have required banks to strengthen their balance sheets. Uplifts to credit ratings for sovereign support have now been largely removed. The credit rating agencies have also changed their methodologies to focus more on loss absorbing capital, effectively shareholders' funds. The credit rating agencies have now completed many of their reviews and as a result of banks strengthening their balance sheets, many of the negative outlooks that were placed on banks did not actually result in downgrades.

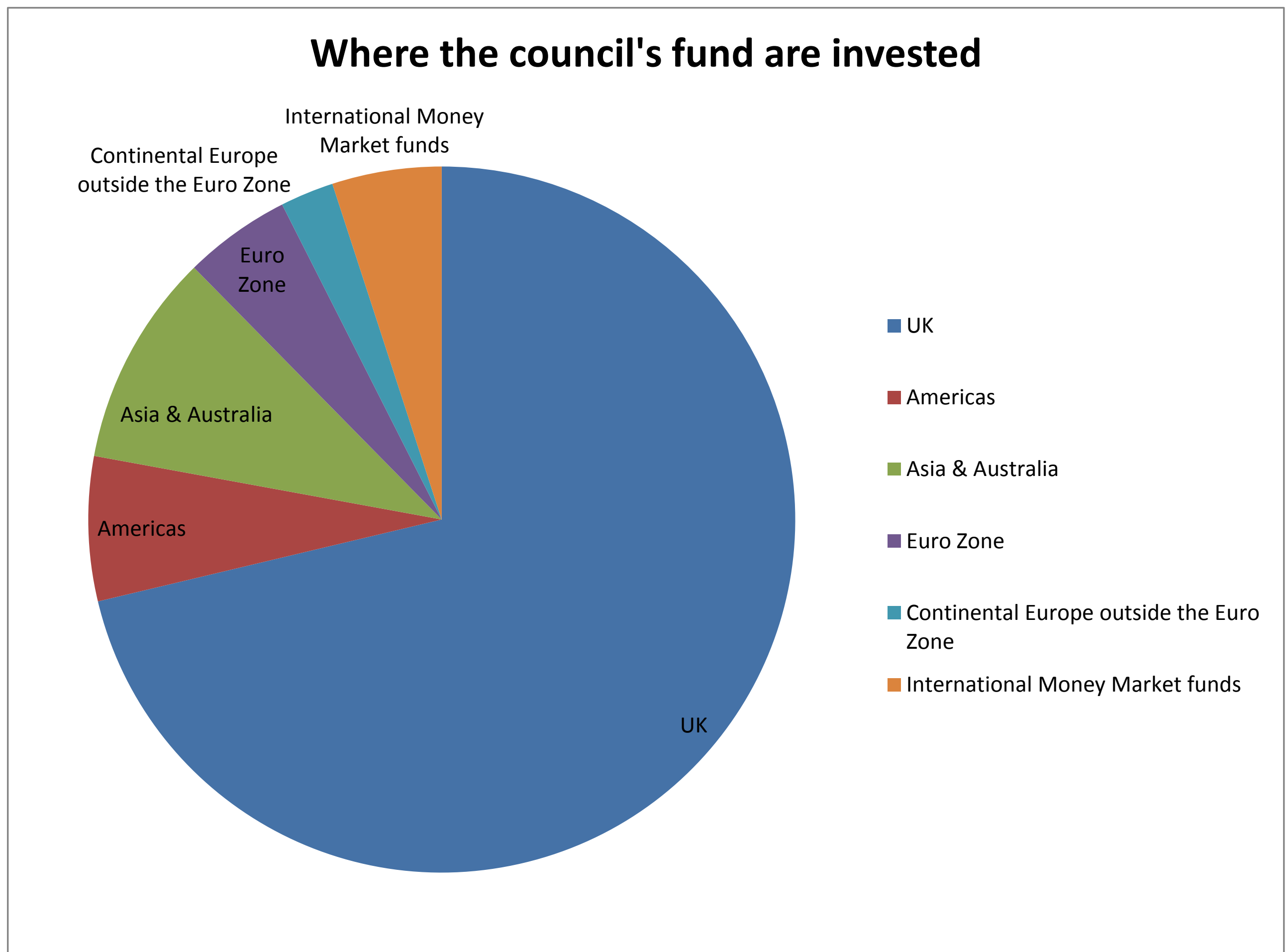
It is recommended that the new counter parties identified be added to the Council's investment counter party list and that the investment limits be revised to take account of any changes to counter party's credit ratings.

10. SECURITY OF INVESTMENTS

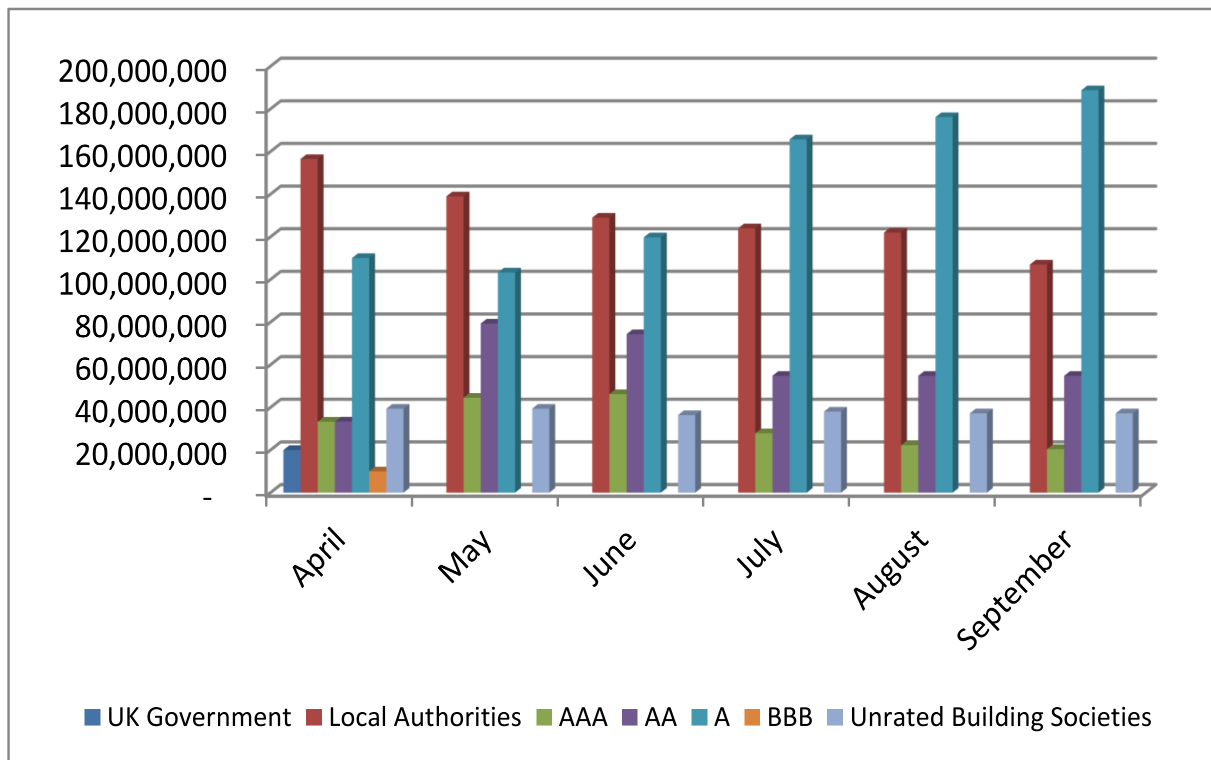
The risk of default has been managed through limiting investments in any institution to £30m or less depending on its credit rating and spreading investments over countries and sectors.

At 30 September 2015 the City Council had on average £5.8m invested with each institution.

The chart below shows where the Council's funds were invested at 30 September 2015.



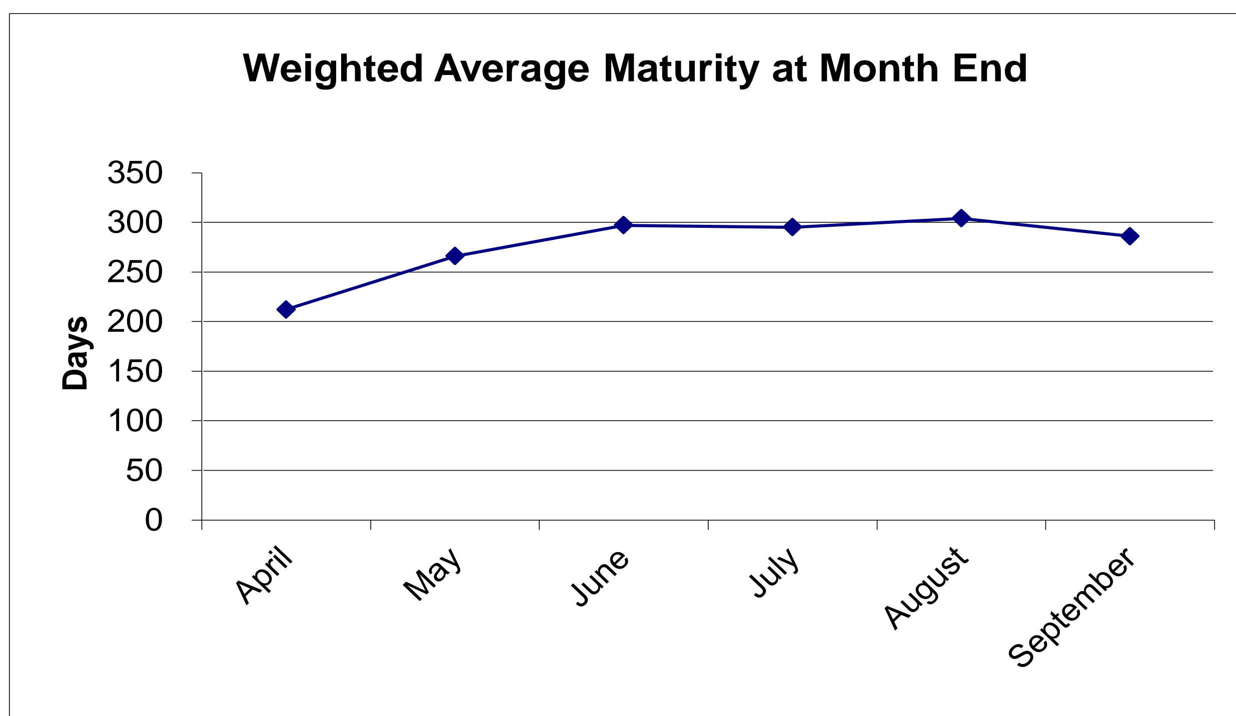
The chart below shows how the Council's investment portfolio has changed in terms of the credit ratings of investment counter parties over the first six months of 2015/16.



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

11. LIQUIDITY OF INVESTMENTS

The weighted average maturity of the City Council's investment portfolio started at 212 days in April and increased to 297 days in June as suitable investments opportunities became available for the increased level of cash in the first quarter of the year. Since June the weighted maturity of the investment portfolio has been fairly stable. This is shown in the graph below.



The 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 30 September £20.4m 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.

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 on 17 March 2015 is shown below.

Maturing after	Limit £m	Actual £m
31/3/2016	243	159
31/3/2017	231	70
31/3/2018	228	5

12. 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 limits set by the City Council on 17 March 2015 is shown below.

	Limit **£m**	**Actual** **£m**
Maximum Projected Gross Borrowing – Fixed Rate	395	384
Minimum Projected Gross Investments – Fixed Rate	(91)	(166)
Fixed Interest Rate Exposure	304	218

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 and 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 limits set by the City Council on 17 March 2015 is shown below.

	Limit £m	Actual £m
Minimum Projected Gross Borrowing – Variable Rate	-	-
Maximum Projected Gross Investments – Variable Rate	(358)	(242)
Variable Interest Rate Exposure	(358)	(242)

The City Council is particularly exposed to interest rate risk because all the City Council's debt is made up of fixed rate long term loans, but most of the City Council's investments are short term. Future movements in the Bank Base Rate tend to affect the return on the Council's investments, but leave fixed rate long term loan payments unchanged. This could favour the City Council if short term interest rates rise.

The risk of a 0.5% change in interest rates to the Council is as follows:

Effect of +/- 0.5% Rate Change	**2015/16 (Part Year)** £'000	**2016/17** £'000	**2017/18** £'000
Long Term Borrowing	-	2	55
Investment Interest	(123)	(641)	(780)
Net Effect of +/- 0.5% Rate Change	**(123)**	**(639)**	**(725)**