**LANCASHIRE COMBINED FIRE AUTHORITY**
**RESOURCES COMMITTEE**
Meeting to be held on 28 June 2017

**YEAR END TREASURY MANAGEMENT OUTTURN 2016/17**
**(Appendix 1 refers)**

Contact for further information:
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**Executive Summary**

The report sets out the Authority's borrowing and lending activities during 2016/17. All borrowing and investment activities undertaken throughout the year are in accordance with the Treasury Management Strategy 2016/17, and are based on anticipated spending and interest rates prevailing at the time.

**Recommendation**

The Authority are asked to note and endorse the outturn position report

**Information**

In accordance with the updated CIPFA Treasury Management code of practice and to strengthen members' oversight of the Authority's treasury management activities, the Resources Committee receives regular updates on treasury management issues including a mid-year report and a final outturn report. Reports on treasury activity are discussed on a quarterly basis with Lancashire County Council Treasury Management Team and the Director of Corporate Services and the content of these reports is used as a basis for this report to the Committee.

**Economic Overview**

Treasury Management activity is influenced by the actual and forecast economic position. The economic situation in the year was largely dominated by the uncertainty about the short and medium term implications of the decision in June 2016 to leave the European Union. In response to the risk of reduced economic growth the Bank of England Monetary Policy Committee initiated substantial monetary policy easing at its August meeting. This included a cut in Bank Rate to 0.25%, further gilt and corporate bond purchases (QE) and cheap funding for banks (Term Funding Scheme) to maintain the supply of credit to the economy.

The year has seen steady economic growth although the final quarter is at a lower rate with the quarterly rates being:

| Quarter ended : | GDP growth (%) |
|---|---|
| June 2016 | 0.6 |
| September 2016 | 0.5 |
| December 2016 | 0.7 |
| March 2017 (provisional) | 0.2 |

Inflation remained low in the first half of 2016 but there has been signs of this increasing towards the end of the year with inflation as measured by RPIH being at 2.3% at March 2017. However, since the referendum vote the value of sterling has fallen and this is a significant factor behind the increase in inflation. The unemployment rate dropped to 4.7% in February its lowest level in 11 years.

However, the year has seen significant volatility in the financial markets as a result of both the UK vote to leave the European Union and Donald Trump being elected as President of the USA. As a consequence of the uncertainty Gilt yields fell, Fitch and Standard & Poor's downgraded the UK's sovereign rating to AA and the value of sterling fell. The impact of the negotiations to leave the European Union will be a source of on-going uncertainty.

**Interest Rate Environment**

Short term interest rates continue to be at historically very low levels. As referred to above in response to a potential reduction in economic growth the Bank of England reduced the base rate from 0.5% to 0.25% in August 2016; a level it remained at throughout the rest of the year. The expectation during the year was that interest rates would remain low for the rest of the financial year and beyond. This is still the case with Lancashire County Council's Treasury Management advisors, Arlingclose Treasury Consultants, not forecasting an increase up to June 2020.

**Cash Flow**

Cash flow predictions are made on a rolling basis in order to ensure that the Authority has sufficient funds to meet its day to day requirements and also inform investment and borrowing decisions.

Appendix 1 shows the actual cash flows over the last 12 months, split between fixed deposits and the call account.

Broadly speaking it can be seen that the cash flow projections are reasonably accurate. The cash flow position, along with the interest rate environment, form part of the regular discussions between the Director of Corporate Services and the Lancashire County Council Treasury Management Team, in order to inform future decisions on borrowing and investments.

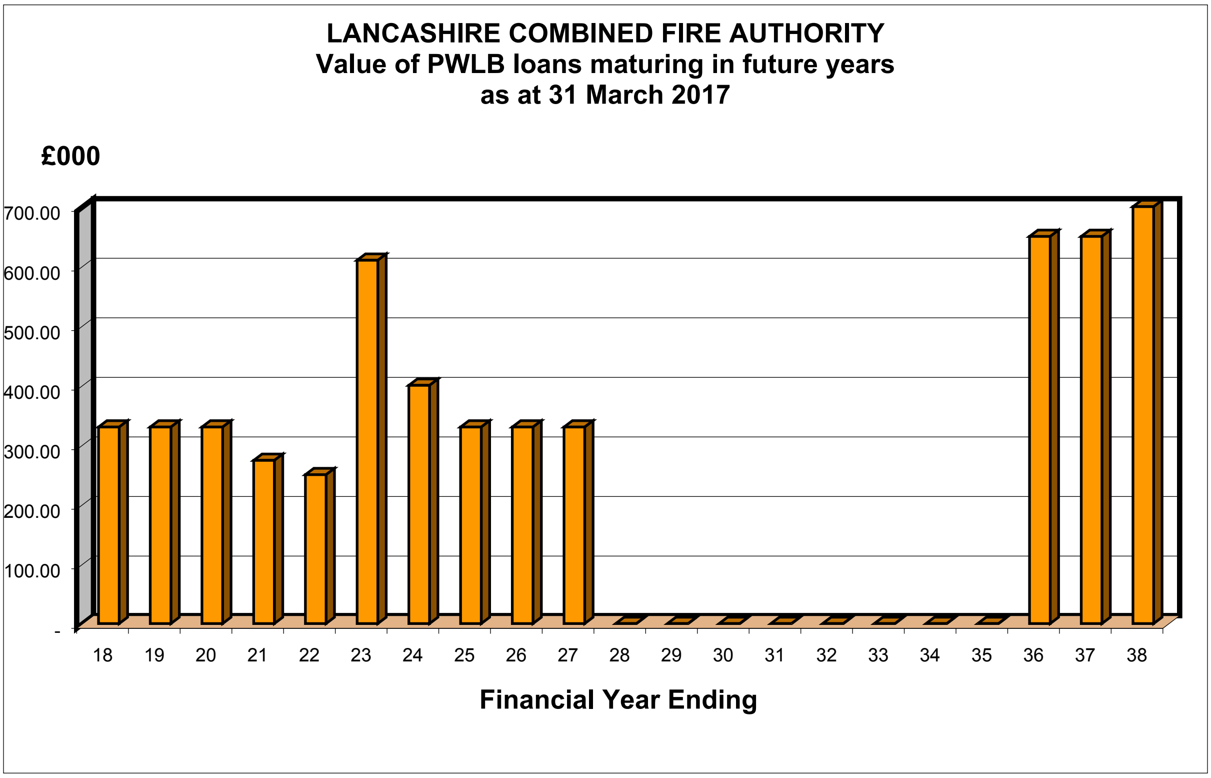
**Borrowing**

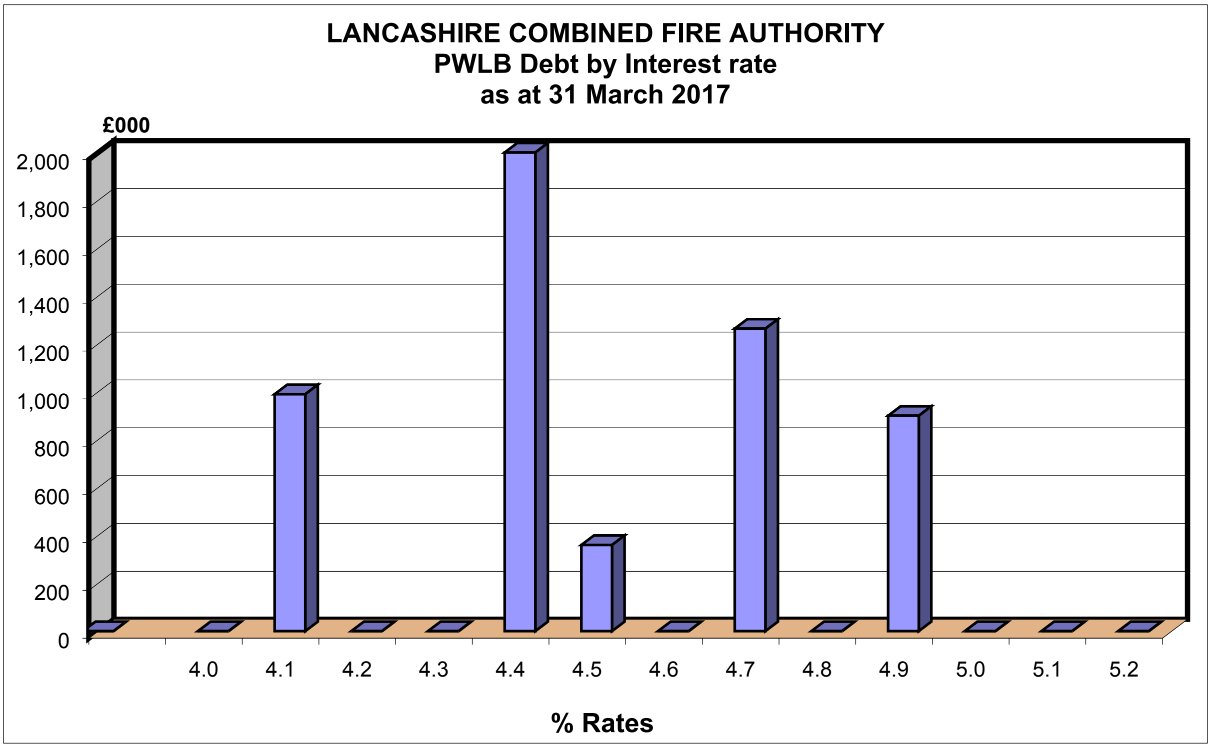
There has been no new borrowing undertaken in the year. This is in line with the continuation of the policy of using cash balances to fund capital expenditure which has resulted in no new borrowing being undertaken since 2007. In addition, the Fire Authority's has a policy to set aside monies in the form of statutory and voluntary Minimum Revenue Provisions (MRP) in order to reduce borrowing requirements and enable the repayment of debt as it matures. The estimated balance at 31/3/16 was £5.682m and therefore during the year a maturing debt of £0.250m was repaid.

An exercise was undertaken to see if it was cost effective to repay some of the other PWLB loans early but with the premium that would have been incurred this was not deemed to be cost effective. Therefore the borrowing position is:

| | 2016/17 |
|---|---|
| | £'000 |
| Borrowing at 31 March 2016 | 5,764 |
| Repayment of Maturing Debt | 250 |
| New Borrowing | - |
| Borrowing at 31 March 2017 | **5,514** |

The charts below show the current maturity profile and interest rate profile of the Authority's borrowings.






Total interest payable on PWLB borrowing amounts to £0.260m, which equates to an average interest rate of 4.55%.

**Investments**

Both the CIPFA Code and the CLG Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. Throughout the year when investing money the key aim was to strike an appropriate balance between risk and return.

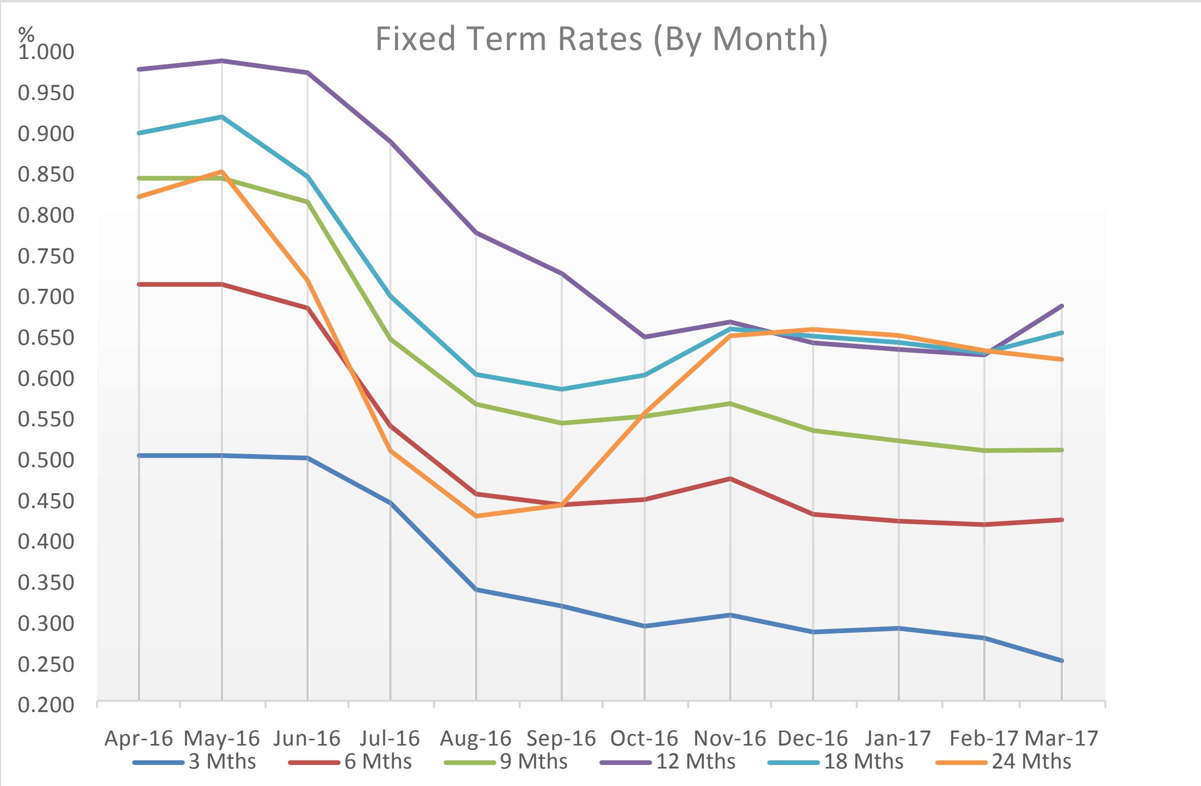
In order to reduce credit risk to the Authority, Lancashire County Council (credit rating by Moodys AA2) is the main counterparty for the Authority's investments via the operation of a call account. However the Treasury Management Strategy does include other high quality counterparties. In accordance with this policy, two long term investments are held with UK local authorities as outlined below:

| Start Date | End Date | Principal | Rate | Annual Interest |
|---|---|---|---|---|
| 30/6/14 | 28/6/19 | £5,000,000 | 2.4% | £120,000 |
| 31/7/14 | 31/7/17 | £5,000,000 | 1.6% | £80,000 |

The call account provided by Lancashire County Council paid the base rate throughout 2016/17. Each working day the balance on the Authority's current account is invested in this to ensure that the interest received on surplus balances is maximised. The average balance in this account during the year was £32.4m earning interest of £0.105m.

The overall interest earned during this period was £0.305m at a rate of 0.72% which compares favourably with the benchmark 7 day notice index which averages 0.36% over the same period.

The chart below shows the interest rates for different investment maturities available during the year. Although indicative of the rates available they might have been offered by lenders who do not meet the credit rating criteria of the Authority's policy.




All of these investments are made in accordance with the current Treasury Management Strategy and the CIPFA treasury management code of practice.

Cash flow and interest rates continue to be monitored by the Director of Corporate Services and the County Council's treasury management team, and when rates are felt to be at appropriate levels further term deposits will be placed.

**Prudential Indicators**

In order to control and monitor the Authority’s treasury management functions, a number of prudential indicators are determined against which performance may be measured. The revised indicators for 2016/17 are shown in the table over the page alongside the actual outturn position.

| | Revised | Actual |
|---|---|---|
| **Adoption of the CIPFA Code of Practice for Treasury Management** | Adopted | Adopted |
| **Authorised limit for external debt** | £000 | £000 |
| A prudent estimate of total external debt, which does not reflect the worst case scenario, but allows sufficient headroom for unusual cash movements | | |
| Borrowing | 7,800 | 5,514 |
| Other long-term liabilities – these relate to vehicle finance leases and the PFI agreements | 15,400 | 14,651 |
| Total | 23,200 | 20,165 |
| **Operational boundary for external debt** | | |
| A prudent estimate of debt, but no provision for unusual cash movements. It represents the estimated maximum external debt arising as a consequence of the Authority's current plans | | |
| Borrowing | 6,800 | 5,514 |
| Other long-term liabilities – these relate to vehicle finance leases and the PFI agreements | 14,900 | 14,651 |
| Total | 21,700 | 20,165 |
| **Upper limit for fixed interest rate exposure** | | |
| Borrowing | 100% | 100% |
| Investments | 100% | 25.6% |
| **Upper limit for variable rate exposure** | | |
| Borrowing | 25% | Nil |
| Investments | 100% | 74.4% |
| **Upper limit for total principal sums invested for over 364 days** (per maturity date) | 25,000 | 5,000 |
| **Maturity structure of debt** | **Upper/ Lower Limits** | **Actual** |
| Under 12 months | 30%/nil | 5.98 |
| 12 months and within 24 months | 30%/nil | 5.98 |
| 24 months and within 5 years | 50%/nil | 15.49 |
| 5 years and within 10 years | 80%/nil | 36.27 |
| 10 years and above | 90%/nil | 36.27 |
| Historically the above maturity structure has proved to be sound. It aims to produce a stable debt structure over the longer-term whilst permitting the exploitation of favourable interest rates at the short end of the market if they arise. | | |

**Financial Implications**

The following table summarises the Financing costs for the Authority, comparing actual with budget:-

| | Revised Budget | Actual | Reason for variance |
|---|---|---|---|
| Interest Payable on PWLB loans | £0.263m | £0.260m | In line with revised budget |
| Interest Receivable on call account and fixed term investments | (£0.378m) | (£0.305m) | We have generated £73k less investment income than budgeted reflecting the reduction in the call account interest rate during quarter two following the reduction in the Bank of England base rate. |
| Minimum Revenue Provision re PWLB loans | £0.028m | £0.028m | In line with revised budget |
| Net financing income from Treasury Management activities* | (£0.087m) | (£0.017m) | |

*There are financing costs associated with vehicle finance leases and the PFI agreements, which are not included in the balances above as they are not the result of Treasury Management activities.

**Human Resource Implications**

None

**Equality and Diversity Implications**

None

**Business Risk Implications**

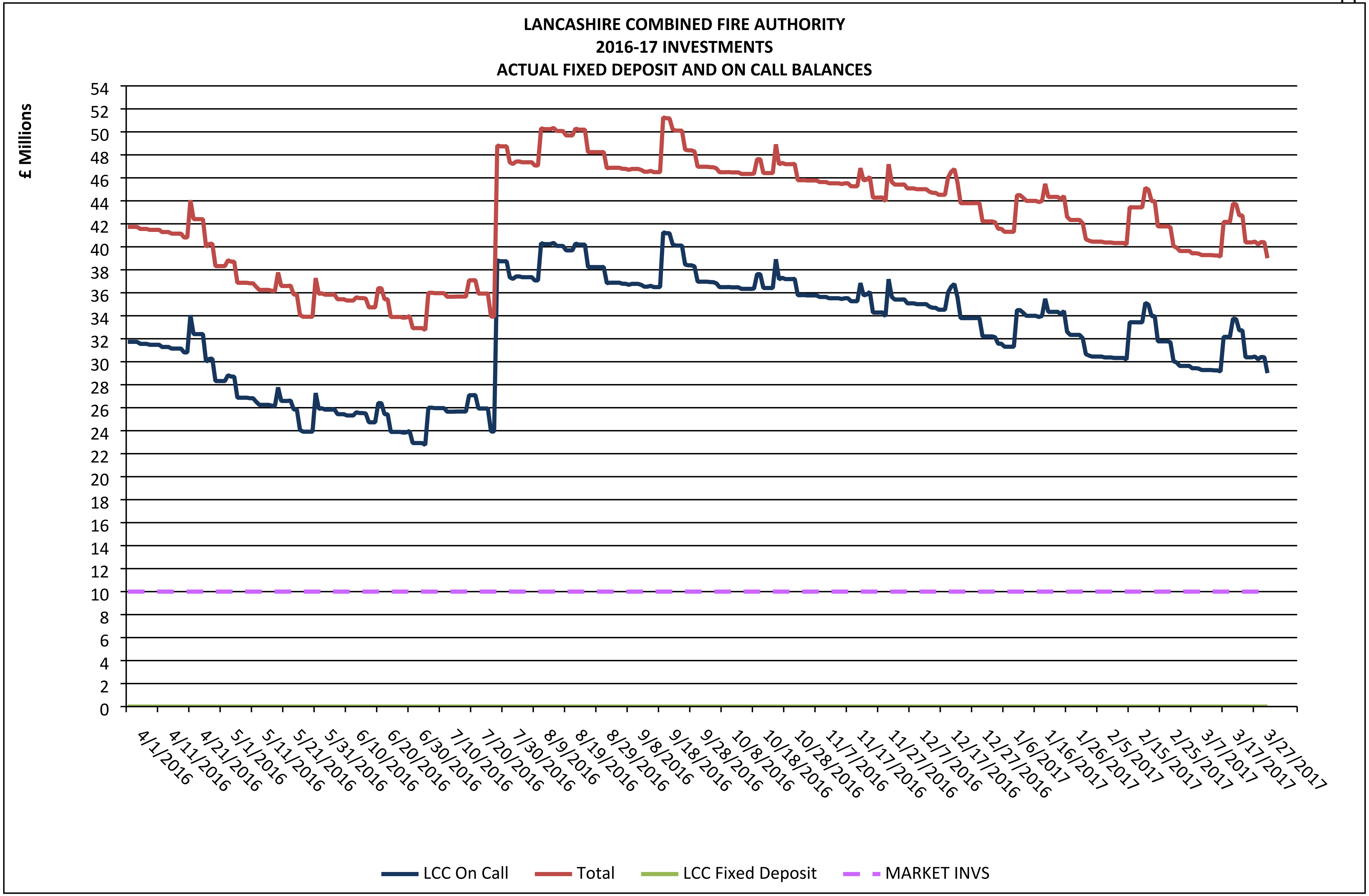
The Treasury Management Strategy is designed to maximise interest earned, minimise interest paid whilst maintaining an acceptable level of risk. The reviews of performance provide members with an assurance that this has been complied with.

**Environmental Impact**

None

**Local Government (Access to Information) Act 1985**
**List of Background Papers**

| Paper | Date | Contact |
|---|---|---|
| Treasury Management Strategy 2016/17 | February 2016 | Keith Mattinson, Director of Corporate Services |
| SORP and Guidance | February 2017 | Keith Mattinson, Director of Corporate Services |
| Reason for inclusion in Part II, if appropriate: | | |


LANCASHIRE COMBINED FIRE AUTHORITY
2016-17 INVESTMENTS
ACTUAL FIXED DEPOSIT AND ON CALL BALANCES
£ Millions
54
52
50
48
46
44
42
40
38
36
34
32
30
28
26
24
22
20
18
16
14
12
10
8
6
4
2
0
4/1/2016
4/11/2016
4/21/2016
5/1/2016
5/11/2016
5/21/2016
5/31/2016
6/10/2016
6/20/2016
6/30/2016
7/10/2016
7/20/2016
7/30/2016
8/9/2016
8/19/2016
8/29/2016
9/8/2016
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9/28/2016
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11/7/2016
11/17/2016
11/27/2016
12/7/2016
12/17/2016
12/27/2016
1/6/2017
1/16/2017
1/26/2017
2/5/2017
2/15/2017
2/25/2017
3/7/2017
3/17/2017
3/27/2017
LCC On Call
Total
LCC Fixed Deposit
MARKET INVS