HAMBLETON DISTRICT COUNCIL

Report To: Cabinet
2 December 2014

Subject: **2014/15 Q2 CAPITAL MONITORING AND TREASURY MANAGEMENT MID YEAR REVIEW REPORT**

All Wards
Portfolio Holder for Economic Development and Finance: Councillor P R Wilkinson

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1.0 PURPOSE AND BACKGOUND:

1.1 The purpose of this report is to provide the quarter 2 update at 30 September 2014 on the progress of the capital programme 2014/15 and the treasury management position. A full schedule of the capital programme 2014/15 schemes is attached at Annex A, together with the relevant update on progress of each scheme.

1.2 Capital expenditure is intrinsically linked with treasury management as the way that the capital programme is funded, directly effects the treasury management arrangements of the Council. This Council currently does not borrow for a capital purpose; instead capital expenditure is funded by grants, receipts and reserves. The use of the Council's funds affects the daily treasury management cash flow position, the requirement to investment these surplus funds and the income earned.

2.0 CAPITAL PROGRAMME SUMMARY:

2.1 The 2014/15 capital programme was approved by Cabinet at quarter 1 on 2 September 2014 at £2,802,190.

2.2 A net decrease to the capital programme of £258,763 is detailed in this Quarter 2 monitor that results in a revised capital programme budget of £2,543,427. The Capital programme is attached at Annex A.

2.3 The net decrease of £258,763, to be approved in this report, is made up of:-
(a) decrease in expenditure from re-profiling of £331,000 from this year to 2015/16
(b) increase in expenditure of £74,216 supported from Council reserves;
(c) reduction in scheme expenditure of £1,979.

2.4 Table 1 below outlines the variances reported against each portfolio area.

Portfolio	Current Approved Expenditure Q1 £	Revised projected Outturn Q2 £	Variance Increase/ (decrease) £	Budget re-profiled (to) 2015/16 £	Request for additional funding £	Funding no longer required £
Environmental & Planning Services	321,379	340,029	18,650	-	18,650	-
Customer & Leisure	877,347	587,068	(290,279)	(331,000)	42,700	(1979)
Support Services	1,603,464	1,616,330	12,866	-	12,866	-
Total	**2,802,190**	**2,543,427**	**(258,763)**	**(331,000)**	**74,216**	**(1,979)**

Table 1: Capital Programme Q2 2014/15

2.5 To 30 September 2014 capital expenditure of £568,936 had been incurred or committed representing 22.4% of the revised Q2 capital programme position. Schemes are under development and at Q3 an increase volume of works are expected to be committed prior to the end of the financial year.

2.6 The proposed changes to the Capital Programme, detailed for each of the 3 portfolio areas, are attached at Annex B.

3.0 FUNDING THE CAPITAL PROGRAMME:

3.1 For 2014/15, at Quarter 2, the capital programme of £2,543,427 is being funded from £285,704 external grants/contributions and £2,257,723 from reserves.

3.2 The external grants contributions of £285,704 are £166,277 Government Grant for Disabled Facilities grant, £50,000 S106 funding towards Sowerby Sports Village, £19,000 towards Hambleton All Weather Pitch and £50,427 as a result of 46% of the Bedale All Weather Pitch scheme being funded by a contribution from the Football Foundation

3.3 The capital receipts estimated to be received during 2014/15 is £857,707.

3.4 Therefore at year end in accordance with accounting practice the capital programme will be financed using all available in year funding prior to using the Council's reserves. At quarter 2 it is estimated that £1,400,016 of reserve funding will be used from the capital receipts or unapplied grants reserves.

3.5 The overall funding position continues to be closely monitored to ensure the overall capital programme remains affordable and sustainable over the 10 year approved capital plan. Analysis of the funding of the 10 year capital programme will be provided along with the financial strategy and Capital Programme 2015/16, when approval is required prior to the beginning of the new financial year.

3.6 It should be noted that this report reflects the capital programme position at Q2 as if approval has been agreed by Cabinet. This is detailed in the recommendations below.

4.0 TREASURY MANAGEMENT MID YEAR REVIEW 2014/15

4.1 The Treasury Management Mid-Year 2014/15 is attached at Annex C and provides Members with an update on the:
(a) treasury management position
(b) economy and interest rates
(c) annual investment strategy
(d) investment performance
(e) borrowing position
(f) Compliance with prudential and treasury indicators

4.2 The annual investment strategy has changed in this mid-year review in relation to the credit rating agencies approach to credit ratings criteria. The three main rating agencies (Fitch, Moody's and Standard & Poor's) have, through much of the financial crisis, provided some institutions with a ratings "uplift" due to implied levels of sovereign support. More recently, in response to the evolving regulatory regime, the agencies have indicated they may remove these "uplifts", making part of the agencies approach to credit ratings redundant.

4.3 The credit rating agencies have Long and Short Term rates to define their credit ratings and in addition Support, Financial Strength and Viability ratings. It is these later categories that are now redundant. The change in this process may occur during this financial year, although the actual timing of the changes is still subject to discussion; however, this does mean immediate changes are required to the credit methodology in this report.

4.4 As a result of these rating agency changes, this element of Capita Asset Services (the Council's treasury management advisers) future credit rating methodology will focus solely on the Short and Long Term ratings of an institution. Rating Watch and Outlook information will continue to be assessed where it relates to these categories. This is the same process for Standard & Poor's that has always been taken, but a change to the use of Fitch and Moody's ratings. Further, the credit rating process will continue to utilise Credit Default Swap prices (as has been the case in the past) as an overlay to ratings in the new methodology.

4.5 The investment position at Quarter 2 was £30,070,000 with an average interest rate return of 0.79%; this was 0.44% higher than the 7 day market rate at 0.35%. When comparing this with District Councils at 0.69% that are monitored by Capita Asset Services, the Council's return was 0.10% greater. For surplus funds invested for 3 months or more, a return of 0.85% was achieved which was 0.43% greater than the 3 month benchmark at 0.42%.

4.6 The interest rate environment continues to offer investment market rates of return around the Base Rate level of 0.5%. There is some volatility in the market due to the uncertainty as to when the Base Rate will rise due to the global economic environment. Market volatility offers opportunities to seek out higher rates of investment return above Base Rate. The interest earned in 2014/15 is estimated at £300,000 and this is being closely monitored and further information will be provided at Q3. Further information on the economic environment and interest rates is attached at Annex D.

4.7 The Council remains debt free; no borrowing has been taken in 2014/15.

4.8 The Council has operated within the treasury and prudential indicators set out at Annex E. The Director of Resources – S151 Officer - confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2013/14.

5.0 LINK TO COUNCIL PRIORITIES:

5.1 All schemes approved as part of the capital programme have been evaluated against key corporate priorities. Schemes are only undertaken and approved by cabinet in accordance with the Council Plan and supporting project initiation documentation.

5.2 Treasury Management supports all aspects of the Council's priorities as with good management of surplus funds, investment interest earned can be used to support Council services.

6.0 RISK ASSESSMENT:

6.1 There are two main risk associated with the capital programme and treasury management:-

Risk	Implication	Prob	Imp	Total	Preventative action
Capital budgets are not monitored, expenditure is above budget and the funding position is unknown	The Council is unable to control capital expenditure or redirect resources to priority areas	3	5	15	Continue with regular budget monitoring with regular reports to Chief Officers, Management team and Members

Risk	Implication	Prob	Imp	Total	Preventative action
Treasury management investment of surplus funds occurs with unsound institutions	The value of the investment could be lost	3	5	15	Use of treasury management advisers, good investment creditworthiness rating criteria policy approved by Council and regular monitoring reporting to Members

Prob = Probability, Imp = Impact, Score range is Low = 1, High = 5

7.0 FINANCIAL IMPLICATIONS:

7.1 The financial implications are dealt with in the body of the report.

8.0 LEGAL IMPLICATIONS:

8.1 Treasury Management activities and the Capital programme conform to the Local Government Act 2003 and the Council has adopted the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code and the CIPFA Treasury Management Code of Practice.

9.0 EQUALITY/DIVERSITY ISSUES:

9.1 The capital programme seeks to address key equality issues that affect the Council and the public. The main scheme that specifically addressed equalities in the capital programme 2014/15 is the disabled facilities grant scheme.

10.0 RECOMMENDATIONS:

10.1 It is recommended that Cabinet approves and recommends that Council:-

(1) approve the net decrease of £258,763 in the capital programme to £2,543,427 and the detailed capital programme attached at Annex A;

(2) approve all movements in the capital programme +/- £20,000, in accordance with financial regulations, as detailed in Annex B and below:
   a. the increase in capital expenditure of £36,700 for the Footpath Diversion and & Car Park Creation at Leeming Bar.
   b. the decrease in expenditure from re-profiling of £131,000 from this year to 2015/16 for Hambleton All Weather pitch
   c. the decrease in expenditure from re-profiling £200,000 from this year to 2015/16 for Leisure Equipment

(3) note the further overall increases in the capital programme which are individually below £20,000 as detailed in Annex B and cumulatively total £35,537;

(4) note the Capital Funding position - contributions of £285,704, capital receipts of £857,707 and £1,400,016 capital reserves;

(5) note the treasury management activity at Annex C ;

(6) approve the changes to the investment credit ratings process methodology whereby viability, financial strength and support ratings will not be considered as key criteria in the choice of creditworthy investment counterparties; this will continue to ensure the security of the Council's funds; and

(7) note the prudential and treasury indicators at Annex E and that there were no changes at quarter 2 in the mid-year review.

JUSTIN IVES

Background papers: None

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030913 201314 Q1 CapitalMonitoring+TreasuryMgmt

Capital Programme Schemes 2014/15 (including 2013/14 schemes B/Fwd)

Ref:	Responsible Officer	Title:	Original Approved Expenditure 14/15	Schemes rolled Fwd from 2013/14	Approved Changes at Q1 2014/15	Approved Expenditure Revised at Q1 2014/15	Third Party Contribution	Cost to the Council	Expenditure at 30/9/14	Anticipated Expenditure £	Variance	Change in Funding Taken/(Returned) to Capital Reserve	Estimated completion date	Explanation
			£			£	£	£	£	£	£	£		
		Environmental & Planning Services												
1	MJ	Purchase of bins and boxes for refuse and recycling	36,000			36,000		36,000	21,783	36,000	0			Budget will be spent by year end. Final Orders placed.
13	MJ	Disabled Facilities Grants	150,000	80,379		230,379	100,000	130,379	59,597	230,379	0	-66,277		The budget is predicted to be fully spent this year. There has been a change in the agent for this service to Swale Housing Improvement Agency. Currently £175k has been spent or committed.
B/fwd	MJ	Depot - Wash Bay		18,000		18,000		18,000	0	26,000	**8,000**	**8,000**		Increase in funding £8k requested for approval at Q2 Cabinet. This scheme has changed to fully meet the operational needs of Waste and Street Scene. The ground works extents have increased as the whole of the existing washbay will now need to be removed. An additional splash screen has been included to ensure better protection for spray drift. Frost protection to the water supply and additional works to the washing equipment are now included in the scheme. Works due to commence 1 December 2014.
B/fwd	MJ	Waste & Street Scene Clocking System		9,000		9,000		9,000		9,000	0			Anticipated completion date is February 2015, scheme out to tender.
11	MJ	Central depot external lighting improvements	20,000			20,000		20,000	15,460	20,000	0			Project 95% complete, awaiting the completion of the Depot Wash Bay to complete the scheme; anticipated completion date is January 2015.
12	MJ	Central Depot - Security Fencing	8,000			8,000		8,000	0	8,000	0			Tender documentation being prepared. Works due to commence in January 2015.
	MJ	Idox Performance Management Software - Planning								10,650	**10,650**	**10,650**		Increased funding of £10,650 to be approved at Q2. The software (a) gives planning officers an overview of their work and identifies priorities; and (b) creates management reports on individual and team performance. The software supports cultural change, leading to more extensive and more effective performance management and creating opportunities for pro-active self-management.
											0			
		Total Scheme Value Environmental & Planning Services	**214,000**	**107,379**	**0**	**321,379**	**100,000**	**221,379**	**96,841**	**340,029**	**18,650**	**(47,627)**		
		Customer & Leisure Services												
B/Fwd	DG	Thirsk and Sowerby leisure centre improvement scheme		36,227		36,227		36,227	10,258	36,227	0			Retention monies. Continued negotiation with contractor to rectify poor work. HDC Legal services now involved
	DG	Thirsk & Sowerby Sports Village	0		50,000	50,000	50,000	0	30,550	50,000	0			Funded by section 106 as agreed at December cabinet. Conditions survey complete, Planning Application submitted.
	DG	Stokesley Leisure Centre improvement scheme	0		4,349	4,349	0	4,349	4,349	4,349	0	4,349		Retention monies. Continued negotiation with contractor to rectify poor work. HDC Legal services now involved. Slight increase in Budget approved at Q1.
B/Fwd	DG	Bedale Leisure centre improvement scheme		203,296		203,296		203,296	192,427	203,296	0	-50,427		Outdoor floodlit pitch - Work completed. Football Foundation has also provided 46% of the pitch funding at £50,427, therefore Capital reserve returned. Scheme Compete, invoices to be settled.
B/Fwd	DG	CCTV Control Room Upgrade		3,835		3,835		3,835	0	3,835	0			Scheme is ongoing
B/Fwd	DG	CCTV control room upgrade - Wireless Network		71,000		71,000		71,000	0	71,000	0			The Project Initiation Document continues to be developed
B/Fwd	DG	Thirsk New TIC		1337		1,337		1,337	0	1337	0			Retention monies
B/Fwd	DG	Bedale Craft Yard Window		3,975		3,975		3,975	3,975	3,975	0			Works complete
B/Fwd	DG	Evolution Car Park Extension		7,000		7,000		7,000	5,021	5,021	-1,979	-1,979		Works complete. Remaining budget will be returned to the Capital reserve.
	DG	Workspaces - roller shutter doors	0		9,005	9,005		9,005	0	9,005	0	9,005		New doors being installed to increase efficiency, reduced costs and bring doors up to recommended standards for Health & Safety. Approved at Q! cabinet September 2014. The bulk of the work has been completed and the scheme will be finalised at the end of November 2014.
	DG	Footpath Diversion & Car Park Creation Leeming Bar								36,700	**36,700**	**36,700**		Increased funding of £36,700 to be approved at Q2. Opportunity to create this car park and assist economic growth of the area. Revenue savings of £4,100 have been included in the revenue budget 15/16.
	DG	17 Market Place Bird Netting								6,000	**6,000**	**6,000**		Increased funding of £6,000 to improve the damaged building and address H&S issues.
2	DG	Leisure Equipment Lease Buy	200,000			200,000	200,000	0	0	0	**-200,000**			ROLL FWD 15/16. This will form part of the North Northallerton plans which are currently at consultation stage. Full consideration will be given as this project progresses. Presently liaising with Sport England on external funding which will influence when work will be undertaken.
10	DG	Customer Services Web/Intranet Development	100,000			100,000		100,000	25,900	100,000	**0**			This project is expected to deliver during 2014/15 and approval was given at Outturn 15/07/14 Cabinet for £12,210 of this funding to have been utilised during 2013/14. Expected delivery March 2015.
14	DG	Hambleton All Weather Pitch Refurbishment	131,000			131,000	19,000	112,000	0		**-131,000**			ROLL FWD 15/16. This will form part of the North Northallerton plans which are currently at consultation stage. Full consideration will be given as this project progresses. Presently liaising with Sport England on external funding which will influence when work will be undertaken.
15	DG	Stokesley All Weather Pitch Refurbishment	11,000			11,000		11,000	0	11,000	0			Minor works - not yet started. Due later 14/15.
16	DG	Hambleton Leisure Centre Improvement Scheme	20,000	15,323		35,323		35,323	0	35,323	0			Preparatory works for studio (remaining budget in 15/16). Some expenditure incurred on initial assessment/schematics. Scheme needs to take consideration of North Northallerton project and potential for external grant funding. Not yet started
	DG	Hambleton Leisure Centre Fence	0		10,000	10,000		10,000	13	10,000	0	10,000		Work completed - awaiting invoices
		Total Scheme Value Customer & Leisure Services	**462,000**	**341,993**	**73,354**	**877,347**	**269,000**	**608,347**	**272,493**	**587,068**	**-290,279**	**13,648**		
		Support Services												

Capital Programme Schemes 2014/15 (including 2013/14 schemes B/Fwd)

Annex A

Ref:	Responsible Officer	Title:	Original Approved Expenditure 14/15	Schemes rolled Fwd from 2013/14	Approved Changes at Q1 2014/15	Approved Expenditure Revised at Q1 2014/15	Third Party Contribution	Cost to the Council	Expenditure at 30/9/14	Anticipated Expenditure £	Variance	Change in Funding Taken/(Returned) to Capital Reserve	Estimated completion date	Explanation
			£			£	£	£	£	£	£	£		
B/Fwd	JI	Air conditioning - Legislative requirement Corporate	15000	11,862		26,862		26,862		26,862	0			Scheme on-going, review of air conditioning units to identify those in need of priority. Included in 10 year plan as an ongoing scheme for 3 years.
B/Fwd	JI	Public lighting energy reductions		31,088		31,088		31,088	18,727	31,088	0			Part night complete for Public Lighting awaiting Invoices. Car parks still to consider, budget predicted to be spent.
4	JI	Public lighting replacement	51,000	18,816		69,816		69,816	0	69,816	0			Concrete programmed replacement columns to go ahead as well as every day renewals from ageing stock, budget predicted to be spent.
5	JI	Civic Centre - Carpet Replacement	10,000		7,000	17,000		17,000	6,915	17,000	0	7,000		Work complete, awaiting invoices
6	JI	Civic Centre - Internal Painting	6,000			6,000		6,000	5,999	6,000	0			Complete
7	JI	Civic Centre - Window Replacements	10,000			10,000		10,000	0	10,000	0			Members wing to be completed by end of October 14 with rest of programme to be completed by year end.
8	JI	Civic Centre - Backup Generator	40,000			40,000		40,000	0	40,000	0			Generator ordered, installation planned as per revised programme.
9	JI	ICT Improvements	187,030			187,030		187,030	34,480	187,030	0			Complete iworld to Windows Server migration, infrastructure refresh complete. LIVE SQL 2012 has been set up. Itrent decision to be made,
17	DG	All Leisure Centres - Digital Transaction Software	24,000			24,000		24,000	0	24,000	0			Complete purchase order, start project
9	JI	ICT Leisure Improvements	105,670			105,670		105,670	2,375	105,670	0			This will form part of additional capital funded support from ICT. Project started and will be delivered in phases. Current stage is Server preparation, wi-fi installation in Leisure Centres.
9	JI	ICT Information Security/Compliance	6,300			6,300		6,300	0	6,300	0			The legislative PCN requirements to be completed as highlighted in the Health Check report.
9	JI	ICT Customer Excellence	76,000			76,000		76,000	0	76,000	0			Cloud based responsive eform package gas been enabled, start work om eform migration. Further integration work is being identified.
	JI	ICT Finance system split from Richmondshire District Council	0		60,000	60,000		60,000	38,078	60,000	0	60,000		Decision for the Finance system to be split as part of the repatriation from Richmondshire District Council. New Licences and 20 days of consultancy work required. Approval required at Q1 from Cabinet September 2014.
18	JI	Car Park Restatements	45,000			45,000		45,000	0	45,000	0			Tender documentation to be issued in October. On Site in November 2014
19	JI	Car Parks - Thirsk Cobbles	75,000	14,348		89,348		89,348	93,028	95,754	**6,406**	**6,406**		Work complete £2,726 retention to be paid in 2015/16. Additional funding requested to ensure all cobbles were completed under phase 2 of the scheme, as some cobbles were in worse condition than originally anticipated.
20	JI	Bedale Gateway Car Park	160,000			160,000		160,000	0	160,000	0			Work on Scheme documentation suspended, local consultation to be undertaken on principle of car park due to commence in October
21	JI	Adoptions - Thirsk Phases 2 & 3	200,000			200,000		200,000	0	200,000	0			Liaison started with NYCC on scheme requirements.
22	JI	Adoptions - Electric Bollards - Thirsk & Northallerton	40,000			40,000		40,000	0	40,000	0			Liaison started with NYCC to commence on scheme detail in early August.
	JI	Thirsk Market Place Central Area Enhancement	0		10,000	10,000		10,000	0	10,000	**0**	**14,000**		Street Furniture ordered - works to be completed in October
		Structural Repair to Civic Centre Roof								6,460	**6,460**	**6,460**		Structural damage to the Civic Centre roof has resulted in a longstanding leak in the dormer area in room 308 that leeks into room 223. The scheme requires an investigation and for scaffolding to be erected so a formal assessment can be made. Previous attempts have failed to stop the leak.
N/A	JI	Revenue Repairs & Renewals	399,350			399,350		399,350		399,350	0			Revenue Repair & Renewals funded from Reserves
		Total Scheme Support Services	**1,450,350**	**76,114**	**77,000**	**1,603,464**	**0**	**1,603,464**	**199,602**	**1,616,330**	**12,866**	**93,866**		
		Total Capital Approvals 2014/15	**2,126,350**	**525,486**	**150,354**	**2,802,190**	**369,000**	**2,433,190**	**568,936**	**2,543,427**	**-258,763**	**59,887**		

ANNEX B

PROPOSED CHANGES TO THE CAPITAL PROGRAMME:

1.1 The proposed changes to the capital programme, detailed for each of the portfolio areas are listed below:

1.2 Environmental & Planning Services - 2 schemes require adjustment at Quarter 2:-

(a) Depot-Washbay – Increase of £8,000 is required as this scheme has changed to fully meet the operational needs of Waste and Street Scene. The ground works extents have increased as the whole of the existing washbay will now need to be removed. An additional splash screen has been included to ensure better protection for spray drift, also frost protection to the water supply and additional works to the washing equipment Works due to commence 1 December 2014.

(b) Performance Management Software - Funding of £10,650 is requested to be approved at Q2. The software (a) gives planning officers an overview of their work and identifies priorities; and (b) creates management reports on individual and team performance. The software supports cultural change, leading to more extensive and more effective performance management and creating opportunities for pro-active self-management.

1.4 Customer & Leisure Services - 5 schemes require adjustment at Quarter 2:

(a) Evolution Car Park Extension – Funding of £1,979 is no longer required for this scheme and is to be returned to the capital reserve.

(b) Footpath Diversion & Car Park Creation Leeming Bar - Increased funding of £36,700 to be approved at Q2. Opportunity to create this car park and assist economic growth of the area. Revenue savings of £4,100 have been included in the revenue budget 15/16.

(c) 17 Market Place Bird Netting - Increased funding of £6,000 to be approved at Q2. This scheme is required to improve the damaged building and address H&S issues...

(d) Leisure Equipment – Approval is sort at Q2 to re-profile this scheme in to 2015/16. This scheme will form part of the North Northallerton plans which are currently at consultation stage. Full consideration will be given as this project progresses. Presently liaising with Sport England on external funding which will influence when work will be undertaken.

(e) Hambleton All Weather Pitch Refurbishment Approval is sort at Q2 to re-profile this scheme in to 2015/16. The reason is as (d) above.

1.5 Support Services– 2 schemes require adjustment at Quarter 2:-

(a) Car Parks - Thirsk Cobbles – This projected is now completed and additional expenditure is required at £6,406. Additional funding is requested to ensure all cobbles were completed under phase 2 of the scheme, as some cobbles were in worse condition than originally anticipated

(b) Structural Repair to Civic Centre Roof – Additional of funding at £6,460 is requested for approval at Q2. Structural damage to the Civic Centre roof has resulted in a longstanding leak in the dormer area in room 308 that leaks into room 223. The scheme requires an investigation and for scaffolding to be erected so a formal assessment can be made. Previous attempts have failed to stop the leak

1.6 Capital schemes are monitored on a monthly basis and reported to Cabinet quarterly, ensuring that the majority of schemes are held within budget or reported to Council at the earliest opportunity.

1.7 New Schemes added to the capital programme all have supporting Project Initiation Documentation to ensure projects are affordable, sustainable and prudent.

ANNEX C

TREASURY MANAGEMENT POSITION 2014/15 – QUARTER 2

1.0 LEGISLATIVE REQUIREMENT:

1.1 The Council operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operations ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering optimising investment return.

1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.3 Accordingly, treasury management is defined as:

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

1.4 The CIPFA (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management recommends that members be updated on treasury management activities regularly (Treasury Management Strategy Statement, Annual and Mid-year reports, as well as quarterly updates). This report therefore ensures this Council is implementing best practice in accordance with the Code.

1.5 The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This Mid-year report therefore

(a) updates Members on the current treasury management position
(b) updates Members on the changes to the main rating agencies (Fitch, Moody's and Standard & Poor's approach to credit ratings.

1.6 The Council's capital expenditure plans at quarter 2 continue to be financed by either external grants or contributions, capital receipts received in the year or capital reserves. The changes in the capital expenditure plans as detailed in the first half of this report are not financed by borrowing and do not affect the Council's underlying need to borrow.

1.7 In 2014/15 the Council's treasury position (excluding finance leases) is to continue to be debt free. No borrowing has been taken in 2014/15 to date.

1.8 The capital financing requirement, which is the amount of borrowing required to support the capital expenditure programme, is zero for this Council. All capital expenditure as detailed in the paragraphs above is supported from grants, contributions and reserves. The following table shows the treasury management position as at 30 September 2014:

	30 Sept 14 £000's	**Rate %**
Capital Financing Requirement	0	
Borrowing	0	0.0
Investments	30,070	0.79

Table 1: Borrowing and Investment position at 30 September 2014

1.9 The table shows that changes in the capital expenditure programme only affects the treasury management position through the surplus funds that are available to the Council to invest, to earn investment income.

2.0 THE ECONOMY, INTEREST RATES AND TREASURY MANAGEMENT STRATEGY:

2.1 The economic background, interest rate forecast and summary outlook, which sets the environment in which the Council's treasury management operates is attached at Annex D.

3.0 ANNUAL INVESTMENT STRATEGY 2014/15 – Mid Year Review Quarter 2:

3.1 **Investment Policy** – the Council's investment policy is governed by the Department for Communities and Local Government guidance, which was implemented in the Treasury Management Strategy Statement (TMSS) for 2014/15, and includes the Annual Investment Strategy approved by Cabinet on 11 February 2014. This Policy sets out how surplus funds are invested and placed with highly credit rated financial institutions, using Capita Asset Services suggested credit-worthiness approach. This includes the use of Country sovereign credit ratings as well as individual financial institution credit ratings and Credit Default Swap (CDS) overlay information provided by Capita Asset Services.

3.2 The main rating agencies (Fitch, Moody's and Standard & Poor's) have, through much of the financial crisis, provided some institutions with a ratings "uplift" due to implied levels of sovereign support. More recently, in response to the evolving regulatory regime, the agencies have indicated they may remove these "uplifts". This process may commence during this financial year. The actual timing of the changes is still subject to discussion, but this does mean immediate changes to the credit methodology are required.

3.3 It is important to stress that the rating agency changes do not reflect any changes in the underlying status of the institution or credit environment, merely the implied level of support that has been built into ratings through the financial crisis. The eventual removal of implied Government support will only take place when the regulatory and economic environments have ensured that financial institutions are much stronger and less prone to failure in a financial crisis.

3.4 Both Fitch and Moody's provide "standalone" credit ratings for financial institutions. For Fitch, it is the Viability Rating, while Moody's has the Financial Strength Rating. Due to the future removal of sovereign support from institution assessments, both agencies have suggested going forward that these will be in line with their respective Long Term ratings. As such, there is no point monitoring both Long Term and these "standalone" ratings.

3.5 Furthermore, Fitch has already begun assessing its Support ratings, with a clear expectation that these will be lowered to 5, which is defined as "A bank for which there is a possibility of external support, but it cannot be relied upon." With all institutions likely to drop to these levels, there is little to no differentiation to be had by assessing Support ratings.

3.6 As a result of these rating agency changes, the credit element of our future methodology will focus solely on the Short and Long Term ratings of an institution. Rating Watch and Outlook information will continue to be assessed where it relates to these categories. This is the same process for Standard & Poor's that has always been taken, but is a change to the use of Fitch and Moody's ratings. Further, the credit rating process will continue to utilise Credit Default Swap prices as an overlay to ratings in the new methodology.

3.7 The treasury management strategy statement and annual investment strategy sets out the Council's investment priorities as being:-

- Security of capital;
- Liquidity;
- Yield

3.8 The Council's priority is security of its surplus funds when investing with financial institutions. However the Council will always aim to achieve the optimum return (yield) on investments in line with its risk appetite and which is commensurate with proper levels of liquidity and of course security.

3.9 **Investments held by the Council** - in the current economic climate, 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. Indeed, the Funding for Lending scheme has reduced market investment rates even further. The potential for a prolonging of the Eurozone sovereign debt crisis, and its impact on banks, prompts a low risk and short term strategy. Given this risk environment, investment returns are likely to remain low for the foreseeable future.

3.10 The average level of funds available for investment purposes during quarter 2 – 30 September 2014 - was £30,858,880. The level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme. The Council held core cash balances of £28,000,000 at Quarter 2 and £2,070,000 cash flow movement balances. Total investment balance at 30 September 2104 was £30,070,000.

3.11

Benchmark	Benchmark Return	Council Performance	Investment Interest Earned
7 day	0.35%	0.50%	£13,786
3 month	0.42%	0.85%	£108,308

Table 2: Investment performance for quarter 2 – latest information 30 September 2014

3.12 The table shows that the Council monitors its core cash against 3 month LIBID – London Inter bank Investment Rates – and its cash flow investments against the 7 day rate. The Council outperformed the 3 month benchmark by 0.43% and the 7 day benchmark by 0.15%

3.9 The Council's budgeted investment return for 2014/15 was approved at £300,000, this is being closely monitored and further information will be provided at quarter 3.

4.0 BORROWING 2014/15 – Mid Year Review Quarter 2

4.1 The following borrowing information is provided to ensure Members are updated with the interest rates available for borrowing and are kept informed with regards to the current position. Capita Asset Services – the Council's treasury management advisers – 25 year PWLB target rate for new long term borrowing for quarter 4 2014/15 has decreased by 0.1% to 3.90% and for 5 years has decreased by 0.2% to 2.50%.

4.2 As outlined below, the general trend has been a decrease in interest rates during the last six months across longer dated maturity bands, but a rise in the shorter maturities; this reflects in part the expected rise in the Bank rate.

4.3 The table below shows the Public Works Loans Board interest rates which were available for loans during quarter 2 of 2014/15. The Public Works Loans Board is the mechanism by which the Government allows local authorities to borrow at slightly lower interest rates than are available to other institutions. Certainty rates, as detailed in the table, are interest rates available to local authorities if they inform the Government of their borrowing requirements at the beginning of the financial year and are 0.02% (or 20 basis points) below Public Works Loans Board rates. This was introduced by the Government in October 2012.

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.20%	2.48%	3.16%	3.74%	3.72%
Date	08/04/2014	28/08/2014	28/08/2014	01/09/2014	29/08/2014
High	1.49%	2.87%	3.66%	4.30%	4.28%
Date	16/07/2014	03/07/2014	20/06/2014	03/04/2014	02/04/2014
Average	1.35%	2.66%	3.47%	4.10%	4.07%

Table 3: Public Works Loan Board (PWLB) certainty rates, half year ended 30 September 2013

4.3 **Treasury Borrowing** – the Council remains debt free and undertook no external borrowing for cash flow purposes or capital financing purposes in the first six months of 2014/15.

4.4 **Rescheduling of Borrowing** – the Council has no debt and therefore undertook no rescheduling of debt during 2014/15.

4.5 **Repayment of borrowing** – the Council has no external loans and therefore no repayments were necessary.

5.0 COMPLIANCE WITH PRUDENTIAL AND TREASURY INDICATORS:

5.1 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 (affordability limits) were approved in the Treasury Management Strategy Statement by Cabinet on 11 February 2014 and are in compliance with the Council's Treasury Management Practices.

5.2 During the financial year to date the Council has operated within the Treasury and Prudential Indicators approved and are attached at Annex E.

5.3 Officers can confirm that the approved limits within the Annual Investment Strategy were not breached during the quarter ended 30th September 2014.

ANNEX D

1.0 ECONOMIC UPDATE

1.1 Economic performance to date and outlook

1.1.1 U.K

After strong UK Gross Domestic product (GDP) quarterly growth of 0.7%, 0.8% and 0.7% in quarters 2, 3 and 4 respectively in 2013, (2013 annual rate 2.7%), and 0.7% in Q1, 0.9% in Q2 and a first estimate of 0.7% in Q3 2014 (annual rate 3.1% in Q3), it appears very likely that strong growth will continue through 2014 and into 2015 as forward surveys for the services and construction sectors, are very encouraging and business investment is also strongly recovering. The manufacturing sector has also been encouraging though the latest figures indicate a weakening in the future trend rate of growth. However, for this recovery to become more balanced and sustainable in the longer term, the recovery needs to move away from dependence on consumer expenditure and the housing market to exporting, and particularly of manufactured goods, both of which need to substantially improve on their recent lacklustre performance. This overall strong growth has resulted in unemployment falling much faster through the initial threshold of 7%, set by the Monetary Policy Committee (MPC) last August, before it said it would consider any increases in Bank Rate. The Monetary Policy Committee (MPC) has, therefore, subsequently broadened its forward guidance by adopting five qualitative principles and looking at a much wider range of about eighteen indicators in order to form a view on how much slack there is in the economy and how quickly slack is being used up. The Monetary Policy Committee (MPC) is particularly concerned that the current squeeze on the disposable incomes of consumers should be reversed by wage inflation rising back above the level of inflation in order to ensure that the recovery will be sustainable. There also needs to be a major improvement in labour productivity, which has languished at dismal levels since 2008, to support increases in pay rates. Most economic forecasters are expecting growth to peak in 2014 and then to ease off a little, though still remaining strong, in 2015 and 2016. Unemployment is therefore expected to keep on its downward trend and this is likely to eventually feed through into a return to significant increases in pay rates at some point during the next three years. However, just how much those future increases in pay rates will counteract the depressive effect of increases in Bank Rate on consumer confidence, the rate of growth in consumer expenditure and the buoyancy of the housing market, are areas that will need to be kept under regular review.

Also encouraging has been the sharp fall in inflation (Consumer Prices Index (CPI)), reaching 1.2% in September, the lowest rate since 2009. Forward indications are that inflation is likely to fall further in 2014 to possibly 1%. Overall, markets are expecting that the Monetary Policy Committee (MPC) will be cautious in raising Bank Rate as it will want to protect heavily indebted consumers from too early an increase in Bank Rate at a time when inflationary pressures are also weak. A first increase in Bank Rate is therefore expected in Q2 2015 and they expect increases after that to be at a slow pace to lower levels than prevailed before 2008 as increases in Bank Rate will have a much bigger effect on heavily indebted consumers than they did before 2008.

The return to strong growth has also helped lower forecasts for the increase in Government debt by £73bn over the next five years, as announced in the 2013 Autumn Statement, and by an additional £24bn, as announced in the March 2014 Budget - which also forecast a return to a significant budget surplus, (of £5bn), in 2018-19. However, monthly public sector deficit figures have disappointed so far in 2014/15.

1.1.2 U.S

In September, the Federal Reserve continued with its monthly $10bn reductions in asset purchases, which started in December 2013. Asset purchases have now fallen from $85bn to $15bn and are expected to stop on 29th October 2014, providing the economic outlook remains strong. First quarter Gross Domestic product (GDP) figures for the US were depressed by exceptionally bad winter weather, but growth rebounded very strongly in Q2 to 4.6% (annualised).

The U.S. faces similar debt problems to those of the UK, but thanks to reasonable growth, cuts in government expenditure and tax rises, the annual government deficit has been halved from its peak without appearing to do too much damage to growth, although the weak labour force participation rate remains a matter of key concern for the Federal Reserve when considering the amount of slack in the economy and monetary policy decisions.

1.1.3 Eurozone

The Eurozone is facing an increasing threat from weak or negative growth and from deflation. In September, the inflation rate fell further, to reach a low of 0.3%. However, this is an average for all Eurozone countries and includes some countries with negative rates of inflation. Accordingly, the European Central Bank took some rather limited action in June to loosen monetary policy in order to promote growth. In September it took further action to cut its benchmark rate to only 0.05%, its deposit rate to -0.2% and to start a programme of purchases of corporate debt. However, it has not embarked yet on full quantitative easing (purchase of sovereign debt).

Concern in financial markets for the Eurozone subsided considerably during 2013. However, sovereign debt difficulties have not gone away and major issues could return in respect of any countries that do not dynamically address fundamental issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy, (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to Gross Domestic product (GDP) ratios could continue to rise for some countries. This could mean that sovereign debt concerns have not disappeared but, rather, have only been postponed.

1.1.4 China and Japan

Japan is causing considerable concern as the increase in sales tax in April has suppressed consumer expenditure and growth. In Q2 growth was -1.8% q/q and -7.1% over the previous year. The Government is hoping that this is a temporary blip.

As for China, Government action in 2014 to stimulate the economy appeared to be putting the target of 7.5% growth within achievable reach but recent data has raised fresh concerns. There are also major concerns as to the creditworthiness of much bank lending to corporates and local government during the post 2008 credit expansion period and whether the bursting of a bubble in housing prices is drawing nearer.

1.2 Interest rate forecasts

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

	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18
Bank rate	0.50%	0.50%	0.75%	0.75%	1.00%	1.00%	1.25%	1.25%	1.50%	1.50%	1.75%	2.00%	2.25%	2.50%
5yr PWLB rate	2.50%	2.70%	2.70%	2.80%	2.90%	3.00%	3.10%	3.20%	3.30%	3.40%	3.50%	3.50%	3.50%	3.50%
10yr PWLB rate	3.20%	3.40%	3.50%	3.60%	3.70%	3.80%	3.90%	4.00%	4.10%	4.10%	4.20%	4.20%	4.30%	4.30%
25yr PWLB rate	3.90%	4.00%	4.10%	4.30%	4.40%	4.50%	4.60%	4.70%	4.70%	4.80%	4.80%	4.90%	4.90%	5.00%
50yr PWLB rate	3.90%	4.00%	4.10%	4.30%	4.40%	4.50%	4.60%	4.70%	4.70%	4.80%	4.80%	4.90%	4.90%	5.00%

Capita Asset Services undertook a review of its interest rate forecasts on 24 October. During September and October, a further rise in geopolitical concerns, principally over Ukraine but also over the Middle East, plus fears around Ebola and an accumulation of dismal growth news in most of the ten largest economies of the world and also on the growing risk of deflation in the Eurozone, had sparked a flight from equities into safe havens like gilts and depressed Public Works Loan Board (PWLB) rates. However, there is much volatility in rates as news ebbs and flows in negative or positive ways. This latest forecast includes a first increase in Bank Rate in quarter 2 of 2015.

Our Public Works Loan Board (PWLB) forecasts are based around a balance of risks. However, there are potential upside risks, especially for longer term Public Works Loan Board (PWLB) rates, as follows: -

- A further surge in investor confidence that robust world economic growth is firmly expected, causing a flow of funds out of bonds and into equities.

- UK inflation being significantly higher than in the wider European Union and US, causing an increase in the inflation premium inherent to gilt yields.

Downside risks currently include:

- The situation over Ukraine poses a major threat to the Eurozone and world growth if it was to deteriorate into economic warfare between the West and Russia where Russia resorted to using its control over gas supplies to Europe.

- Fears generated by the potential impact of Ebola around the world

- UK strong economic growth is currently mainly dependent on consumer spending and the potentially unsustainable boom in the housing market. The boost from these sources is likely to fade after 2014.

- A weak rebalancing of UK growth to exporting and business investment causing a weakening of overall economic growth beyond 2014.

- Weak growth or recession in the UK's main trading partner - the European Union, inhibiting economic recovery in the UK.

- A return to weak economic growth in the US, UK and China causing major disappointment in investor and market expectations.

- A resurgence of the Eurozone sovereign debt crisis caused by ongoing deterioration in government debt to Gross Domestic product (GDP) ratios to the point where financial markets lose confidence in the financial viability of one or more countries and in the ability of the European Central Bank and Eurozone governments to deal with the potential size of the crisis.

- Recapitalisation of European banks requiring more government financial support.

- Lack of support by populaces in Eurozone countries for austerity programmes, especially in countries with very high unemployment rates e.g. Greece and Spain, which face huge challenges in engineering economic growth to correct their budget deficits on a sustainable basis.

- Italy: the political situation has improved but it remains to be seen whether the new government is able to deliver the austerity programme required and a programme of overdue reforms. Italy has the third highest government debt mountain in the world.

- France: after being elected on an anti austerity platform, President Hollande has embraced a €50bn programme of public sector cuts over the next three years. However, there could be major obstacles in implementing this programme. Major overdue reforms of employment practices and an increase in competiveness are also urgently required to lift the economy out of stagnation.

- Monetary policy action failing to stimulate sustainable growth in western economies, especially the Eurozone and Japan.

- Heightened political risks in the Middle East and East Asia could trigger safe haven flows back into bonds.

- There are also increasing concerns at the reluctance of western central banks to raise interest rates significantly for some years, plus the huge Quantitative Easing measures which remain in place (and may be added to by the European Central Bank in the near future). This has created potentially unstable flows of liquidity searching for yield and, therefore, heightened the potential for an increase in risks in order to get higher returns. This is a return to a similar environment to the one which led to the 2008 financial crisis.

Annex E

Prudential and Treasury Management Indicators

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 (affordability limits) are included in the approved Treasury Management Strategy Statement by Cabinet on 18 March 2014

The main purpose of the indicators is to control how much a Council needs to borrow and as this Council is debt free, the majority of the prudential indicators are nil.

1. PRUDENTIAL INDICATORS	**2014/15**	**2014/15**
Extract from budget and rent setting report	**Original Budget**	**Actual Q2**
	£'000	**£'000**
Capital Expenditure	2,126	2,543
Ratio of financing costs to net revenue stream	Nil	Nil
Net borrowing requirement General Fund		
brought forward 1 April	Nil	Nil
carried forward 31 March	Nil	Nil
in year borrowing requirement	Nil	Nil
Capital Financing Requirement 31 March 2015	Nil	Nil
Incremental impact of capital investment decisions	£	£
Increase in Council Tax (band D) per annum	£0.06	£0.06

2. TREASURY MANAGEMENT INDICATORS	**2014/15**	**2014/15**
	original	**actual**
	£'000	**£'000**
Authorised Limit for external debt -		
borrowing	£5,000	£5,000
other long term liabilities	£1,000	£1,000
TOTAL	£6,000	£6,000
Operational Boundary for external debt -		
borrowing	£4,000	£4,000
other long term liabilities	£600	£600
TOTAL	£4,600	£4,600
Actual external debt	£0	£0
Upper limit for fixed interest rate exposure		
Net principal re fixed rate investments	90%	90%
Upper limit for variable rate exposure		
Net principal re variable rate investments	50%	50%
Upper limit for total principal sums invested for over 364 days (per maturity date)	£10,000	£10,000

Maturity structure of fixed rate borrowing during 2014/15	upper limit	lower limit
under 12 months	0%	100%
12 months and within 24 months	0%	0%
24 months and within 5 years	0%	0%
5 years and within 10 years	0%	0%
10 years and above	0%	0%