Midlothian

Council
Tuesday 28 June 2016

Annual Treasury Management Report 2015/16

Report by Head of Finance & Integrated Service Support

1. Purpose of Report

The purpose of the report is to inform members of the Treasury Management activity undertaken in 2015/16 and the year end position.

2. Background

The Council has adopted the Code of Practice for Treasury Management in Local Authorities published by the Chartered Institute of Public Finance and Accountancy and complies with its requirements which include an annual Treasury Management report on the previous financial year to be presented by 30 September in each year.

A detailed report "*Annual Treasury Management Review 2015/16*" on the activity during 2015/16 is attached as Appendix 1.

The main points arising from treasury activity in 2015/16 were:

- Two new forward starting loans of £10 million each were entered into by the Council, the first UK local authority to transact on this basis. This involves the Council committing to draw down loan funds at a later date at a fixed interest rate that is benchmarked to the current historically low borrowing environment, with minimal cost of carry and hedging against future interest rate movements and thereby represents an extremely viable alternative to traditional PWLB borrowing, adding certainty to the Council's loan portfolio;

- Total new long term borrowing taken in the year amounted to £7.249 million, £0.200 million being a £0.200 million interest free loan from Salix, and £7.049 million sourced from PWLB at the Project Rate (0.40% discount from standard PWLB rate) and thereby taking advantage of historically low PWLB rates;

- The average rate of interest paid on external debt was 3.61% in 2015/16, up from 3.59% in 2014/15;

- The average rate of return on investments was 0.79% in 2015/16, exceeding the benchmark of 0.61% for the twelfth year in succession;

- The internal loans fund rate increased marginally from 3.23% in 2014/15 (2nd lowest in mainland Scotland – see Appendix 1) to 3.28% in 2015/16, which is again expected to be one of the lowest when benchmarked against all mainland Authorities in Scotland;

- Were the internal loans fund rate to have equated to the Scottish weighted average of 4.49%, this would have generated loan charges in 2015/16 of £18.3m. The Council's actual 2015/16 loan charges for General Services and HRA were £15.2m, representing a cash saving (compared to the Scotland average) of £3.1m in 2015/16;

- No debt rescheduling was undertaken during 2015/16.

3. Report Implications

3.1. Resources

Although benefits from Treasury Management activity continue to accrue there are no direct financial implications or other resource issues arising from this report.

The loan charges associated with Capital Expenditure and Treasury Management activity during 2015/16 are reported in the Financial Monitoring 2015/16 – General Fund Revenue report elsewhere on today's agenda.

3.2. Risk

As the Council follows the requirements of CIPFA Code of Practice and the Prudential Code there are few risks involved in Treasury Management activities. Those risks that do exist are further controlled through written Treasury Management Practices which define the responsibilities of all staff involved.

3.3. Single Midlothian Plan and Business Transformation

Themes addressed in this report:

☐ Community safety
☐ Adult health, care and housing
☐ Getting it right for every Midlothian child
☐ Improving opportunities in Midlothian
☐ Sustainable growth
☒ Business transformation and Best Value
☐ None of the above

3.4 Impact on Performance and Outcomes

The strategies adopted are an integral part of the corporate aim to achieve Best Value as they seek to minimise the cost of borrowing by exercising prudent debt management and investment. This in turn helps to ensure that the Council's capital expenditure is sustainable in revenue terms.

3.5 Adopting a Preventative Approach

The proposals in this report do not directly impact on the adoption of a preventative approach.

3.6 Involving Communities and Other Stakeholders

Although no external consultation has taken place, cognisance has been taken of professional advice obtained from Sector, the Council's appointed Treasury Consultants.

3.7 Ensuring Equalities

There are no equality issues arising from this report.

3.8 Supporting Sustainable Development

There are no sustainability issues arising from this report.

3.9 IT Issues

There are no IT issues arising from this report.

4. Summary

Treasury Management activity during the year has been effective in minimising the cost of borrowing and maximising investment income within the parameters set by the strategy for the year.

5. Recommendations

It is recommended that the Council:-

a) Note the Treasury Management Annual Report for 2015/16.

Date 31 May 2016

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Appendices:-

Appendix 1: Loans Fund Rate Comparison with other Scottish Local Authorities
Appendix 2: Annual Treasury Management Review 2015/16

Appendix 1:-

Loans Fund Rate Comparison 2014/15

Council	Loans Fund Rate
Dumfries & Galloway	3.21%
Midlothian	3.23%
East Lothian	3.36%
Shetland	3.36%
Perth & Kinross	3.46%
Orkney	3.57%
Falkirk	3.82%
Aberdeen City	3.87%
Fife	3.99%
Inverclyde	4.00%
Dundee City	4.15%
North Lanarkshire	4.25%
West Lothian	4.27%
East Renfrewshire	4.28%
South Lanarkshire	4.44%
Renfrewshire	4.46%
Aberdeenshire	4.50%
Clackmannanshire	4.51%
Stirling	4.62%
Scottish Borders	4.69%
Moray	4.71%
Glasgow City	4.72%
West Dunbartonshire	4.72%
Angus	4.78%
Highland	4.91%
East Ayrshire	4.92%
Argyll & Bute	4.93%
East Dunbartonshire	5.03%
Edinburgh City	5.13%
North Ayrshire	5.23%
South Ayrshire	5.66%
Comhairle Nan Eilean Siar	6.07%
Scottish Weighted Average	4.49%

The Loans Fund Rate combines the interest paid by the Council on money borrowed, with the interest earned by the Council on money invested, along with other charges such as internal interest allowed, premiums written off and treasury-related expenses to arrive at a weighted average "loans fund rate" figure for each authority, as noted in the final column above

Appendix 2

Annual Treasury Management Review 2015/16

Midlothian Council
June 2016

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Annual Treasury Management Review 2015/16

Purpose

This Council is required by regulations issued under the Local Government in Scotland Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2015/16. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

During 2015/16 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 17/02/2015)
- a mid year (minimum) treasury update report (Council 03/11/2015)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

The regulatory environment places responsibility on members for the review and scrutiny of treasury management policy and activities. This report is, therefore, important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.

This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit Committee before they were reported to the full Council.

Executive Summary

During 2015/16, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Prudential and treasury indicators	2014/15 Actual £000	2015/16 Budget £000	2015/16 Actual £000
Capital expenditure:-			
General Fund	11,401	34,773	18,949
HRA	11,888	34,985	12,847
Total	**23,289**	**69,758**	**31,796**
Borrowing Required			
General Fund	254	9,020	200
HRA	7,554	32,303	7,106
Total	**7,808**	**41,323**	**7,306**
Capital Financing Requirement:-			
General Fund	103,675	112,636	99,958
HRA	150,234	183,513	154,053
Total	**253,909**	**296,149**	**254,011**
Gross Borrowing	**-**	**-**	**-**
Investments:-			
Under 1 year	55,891	55,000	68,339
Longer than 1 year	-	-	-
Total	**55,891**	**55,000**	**68,339**

The financial year 2015/16 continued the challenging investment environment of previous years, namely low investment returns and continuing heightened levels of counterparty risk.

With that in mind, the general strategy for any new borrowings required was to balance savings from the utilisation of short-term market money from other UK public sector bodies at rates often available at less than base rate (0.5%), with borrowing from PWLB at historically low rates, particularly at the short-medium end of the curve. This allowed longer-term borrowing to be undertaken when rates were low, whilst continued use of shorter-term borrowing within the overall portfolio continued to add value.

The Council continues to maintain an under-borrowed position, reflecting a strategy to cash-back the majority of the Council’s balance sheet reserves. The Council has sought to source new long-term borrowing from PWLB, taking advantage of the historically low rates on offer and utilising the 0.40%

project rate discount, whilst maintaining an element of shorter-dated temporary borrowing on offer at less than base rate (<0.50%).

The Council also entered into two forward starting loan transactions in the last quarter of the financial year. These involve the Council legally committing now to draw down funds at a pre-defined later date, with the interest rate for these loans fixed and benchmarked competitively against current PWLB spot rates. These loans therefore offer the Council certainty for a chunk of its borrowing requirement over the forthcoming financial years with the fixed rate hedging against the Council's interest rate exposure, while minimising the cost of carry compared to traditional models of borrowing from PWLB in advance.

Prudential and treasury indicators are to be found in the main body of this report. The Head of Finance & Integrated Service Support also confirms that borrowing was only undertaken for a capital purpose and the statutory borrowing limit (the authorised limit), was not breached.

Introduction and Background

This report summarises the following:

- **Section 1**: Capital activity during the year;
- **Section 2**: Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- **Section 3**: Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- **Section 4**: Treasury Management Strategy during 2015/16;
- **Section 5**: Summary of interest rate movements during 2015/16;
- **Sections 6/7**: Detailed debt activity during 2015/16;
- **Sections 8/9**: Detailed investment activity during 2015/16; and
- **Section 10**: Performance Measurement.

1. The Council's Capital Expenditure and Financing 2015/16

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

Table 1: Capital Expenditure + Financing			
	2014/15 Actual £000	2015/16 Budget £000	2015/16 Actual £000
General Fund			
Capital Expenditure	11,401	34,773	18,949
Available Funding	11,147	25,753	18,749
Borrowing Required	**254**	**9,020**	**200**
HRA			
Capital Expenditure	11,888	34,985	12,847
Available Funding	4,334	2,682	5,741
Borrowing Required	**7,554**	**32,303**	**7,106**
General Fund and HRA			
Capital Expenditure	23,289	69,758	31,796
Available Funding	15,481	28,435	24,490
Borrowing Required	**7,808**	**41,323**	**7,306**

2. The Council's Overall Borrowing Need

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and what resources have been used to pay for the capital spend. It represents the 2015/16 unfinanced capital expenditure (see above table), plus prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board [PWLB] or the money markets), or utilising temporary cash resources within the Council.

Reducing the CFR – the Council's underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Scheduled Debt Amortisation (or loans repayment), to reduce the CFR. This is effectively a repayment of the borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

The total CFR can also be reduced by:

- the application of additional capital financing resources (such as unapplied capital receipts); or
- charging more than the minimum loan repayment each year through an additional revenue charge.

The Council's CFR for the year is shown below, and represents a key prudential indicator.

Table 2: Council's Capital Financing Requirement			
	31-Mar-15	2015/16	31-Mar-16
CFR:	Actual	Budget	Actual
	£000	£000	£000
Opening balance	**£ 253,163**	**£ 262,164**	**£ 253,909**
Add Borrowing Required	£ 7,808	£ 41,323	£ 7,306
Less scheduled debt amortisation	£ (7,062)	£ (7,338)	£ (7,204)
Closing balance	**£ 253,909**	**£ 296,149**	**£ 254,011**

Borrowing activity is constrained by prudential indicators for net borrowing and the CFR, and by the authorised limit.

Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2014/15) plus the estimates of any additional capital financing requirement for the current (2015/16) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2015/16. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

Table 3: Council's Gross Borrowing Position			
	31-Mar-15	2015/16	31-Mar-16
	Actual	Budget	Actual
	£000	£000	£000
Gross Borrowing	£ 234,705	£ 285,000	£ 237,272
CFR	£ 253,909	£ 296,149	£ 254,011

The authorised limit – this Council has kept within its authorised external borrowing limit as shown by the table below. Once this has been set, the Council does not have the power to borrow above this level.

The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.

Table 4: Gross Borrowing against Authorised Limit / Operational Boundary	
	2015/16
Authorised limit - borrowing	£336,676
Operational boundary - borrowing	£302,199
Maximum gross borrowing position	£245,224
Average gross borrowing position	£227,095

3. Treasury Position as at 31 March 2016

The Council's debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through Member reporting detailed in the Purpose section of this report, and through officer activity detailed in the Council's Treasury Management Practices. At the beginning and the end of 2015/16 the Council's treasury (excluding borrowing by PFI and finance leases) position was as follows:

Table 5: Treasury Position

	31 March 2015 Principal	Rate/ Return	Average Life (Yrs)	31 March 2016 Principal	Rate/ Return	Average Life (Yrs)
Debt						
Fixed Rate Debt						
PWLB	£ 177,969	4.01%	23.18	£ 179,992	4.06%	23.77
Market	£ 41,736	0.82%	7.61	£ 37,280	0.91%	7.40
Total Fixed Rate Debt	**£ 219,705**	**3.41%**	**20.24**	**£ 217,272**	**3.43%**	**20.65**
Variable Rate Debt						
PWLB	£ -	n/a	n/a	£ -	n/a	n/a
Market	£ 15,000	4.63%	35.71	£ 15,000	4.63%	34.71
Total Variable Rate Debt	**£ 15,000**	**4.63%**	**35.71**	**£ 15,000**	**4.63%**	**34.71**
Total debt/gross borrowing	**£ 234,705**	**3.48%**	**21.22**	**£ 237,272**	**3.51%**	**21.54**
CFR	**£ 253,909**			**£ 254,011**		
Over/ (under) borrowing	**£ (19,203)**			**£ (16,739)**		
Investments						
Fixed Rate Investments						
In House	£ 50,000	0.93%	0.56	£ 54,985	0.94%	0.76
With Managers	£ -	n/a	n/a	£ -	n/a	n/a
Total Fixed Rate Investments	**£ 50,000**	**0.93%**	**0.56**	**£ 54,985**	**0.94%**	**0.76**
Variable Rate Investments						
In House	£ 5,891	0.47%	0.00	£ 13,354	0.50%	0
With Managers	£ -	n/a	n/a	£ -	n/a	n/a
Total Variable Rate Investments	**£ 5,891**	**0.47%**	**0.00**	**£ 13,354**	**0.47%**	**0**
Total Investments	**£ 55,891**	**0.88%**	**0.50**	**£ 68,339**	**0.86%**	**0.61**
Net Borrowing	**£ 178,815**			**£ 168,933**		

The maturity structure of the debt portfolio was as follows:

Table 6: Maturity Structure of Debt Portfolio							
	31-Mar-15		2015/16			31-Mar-16	
	Actual		Original Limits			Actual	
	£000	%	%			£000	%
Under 12 months	£ 41,526	18%	0%	to	50%	£ 38,909	16%
12 months to 2 years	£ 2,029	1%	0%	to	50%	£ 10,031	4%
2 years to 5 years	£ 28,502	12%	0%	to	50%	£ 26,911	11%
5 years to 10 years	£ 10,801	5%	0%	to	50%	£ 3,105	1%
10 years to 20 years	£ 52,214	22%	0%	to	50%	£ 51,633	22%
20 years to 30 years	£ 4,100	2%	0%	to	50%	£ 4,100	2%
30 years to 40 years	£ 60,700	26%	0%	to	50%	£ 60,700	26%
40 years to 50 years	£ 29,834	13%	0%	to	50%	£ 36,883	16%
50 years and above	£ 5,000	2%	0%	to	50%	£ 5,000	2%
Total	**£ 234,706**	**100%**				**£ 237,272**	**100%**

The maturity structure of the investment portfolio was as follows:

Table 7: Maturity Structure of Investment Portfolio		
	31-Mar-15	31-Mar-16
	£000	£000
Investments		
Under 1 Year	£ 55,891	£ 68,339
Over 1 Year	£ -	£ -
Total	**£ 55,891**	**£ 68,339**

The exposure to fixed and variable interest rates on debt was as follows:-

Table 8: Fixed/Variable Interest Rate Exposure of Debt Portfolio							
	31-Mar-15		2015/16			31-Mar-16	
	Actual		Original Limits			Actual	
	£000	%	%			£000	%
Fixed Interest Rate Exposure	£ 219,706	94%	0%	to	100%	£ 217,272	94%
Variable Interest Rate Exposure	£ 15,000	6%	0%	to	30%	£ 15,000	6%
Total	**£ 234,706**	**100%**				**£ 232,272**	**100%**

4. The Strategy for 2015/16

The expectation for interest rates within the treasury management strategy for 2015/16 anticipated low but rising Bank Rate, (starting in quarter 1 of 2016), and gradual rises in medium and longer term fixed borrowing rates during 2016/17. Variable, or short-term rates, were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

In this scenario, the treasury strategy was to postpone borrowing to avoid the cost of holding higher levels of investments and to reduce counterparty risk.

The actual movement in gilt yields meant that the general trend in PWLB rates during 2015/16 was an increase in rates during the first quarter followed by marked bouts of sharp volatility since July 2015 but with an overall dominant trend for rates to fall to historically low levels by the end of the year.

With that in mind, the general strategy for any new borrowings required was to balance savings from the utilisation of short-term market money from other UK public sector bodies at rates often available at less than base rate (0.5%), with borrowing from PWLB at historically low rates. This allowed longer-term borrowing to be undertaken in the middle of the financial year when rates were low, whilst continued use of shorter-term borrowing within the overall portfolio continued to add value.

5. The Economy and Interest Rates

Market expectations for the first increase in Bank Rate moved considerably during 2015/16, starting at quarter 3 2015 but soon moving back to quarter 1 2016. However, by the end of the year, market expectations had moved back radically to quarter 2 2018 due to many fears including concerns that China's economic growth could be heading towards a hard landing; the potential destabilisation of some emerging market countries particularly exposed to the Chinese economic slowdown; and the continuation of the collapse in oil prices during 2015 together with continuing Eurozone growth uncertainties.

These concerns have caused sharp market volatility in equity prices during the year with corresponding impacts on bond prices and bond yields due to safe haven flows. Bank Rate, therefore, remained unchanged at 0.5% for the seventh successive year. Economic growth (GDP) in the UK surged strongly during both 2013/14 and 2014/15 to make the UK the top performing advanced economy in 2014. However, 2015 has been disappointing with growth falling steadily from an annual rate of 2.9% in quarter 1 2015 to 2.1% in quarter 4.

The Funding for Lending Scheme, announced in July 2012, resulted in a flood of cheap credit being made available to banks which then resulted in money market investment rates falling materially. These rates continued at very low levels during 2015/16.

The sharp volatility in equity markets during the year was reflected in sharp volatility in bond yields. However, the overall dominant trend in bond yields since July 2015 has been for yields to fall to historically low levels as forecasts for inflation have repeatedly been revised downwards and expectations of increases in central rates have been pushed back. In addition, a notable trend in the year was that several central banks introduced negative interest rates as a measure to stimulate the creation of credit and hence economic growth.

The ECB had announced in January 2015 that it would undertake a full blown quantitative easing programme of purchases of Eurozone government and other bonds starting in March at €60bn per month. This put downward pressure on Eurozone bond yields. There was a further increase in this programme of QE in December 2015. The anti-austerity government in Greece, elected in January 2015 eventually agreed to implement an acceptable programme of cuts to meet EU demands after causing major fears of a breakup of the Eurozone. Nevertheless, there are continuing concerns that a Greek exit has only been delayed.

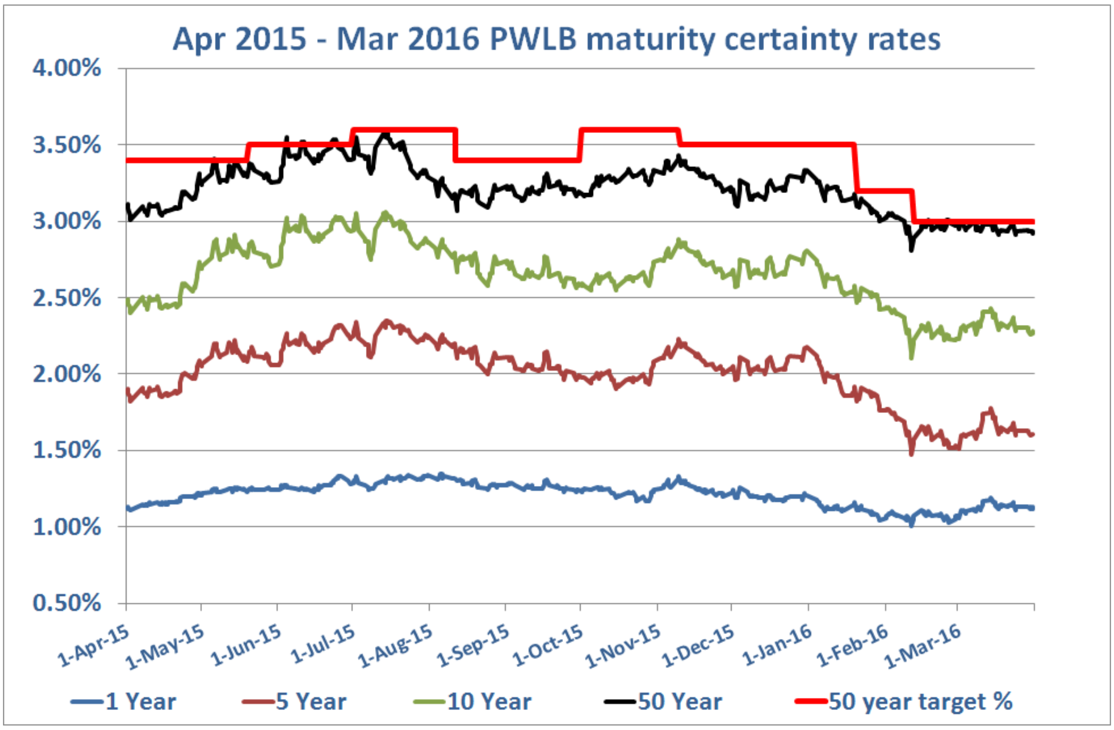
As for America, the economy has continued to grow healthily on the back of resilient consumer demand. The first increase in the central rate occurred in December 2015 since when there has been a return to caution as to the speed of further increases due to concerns around the risks to world growth.

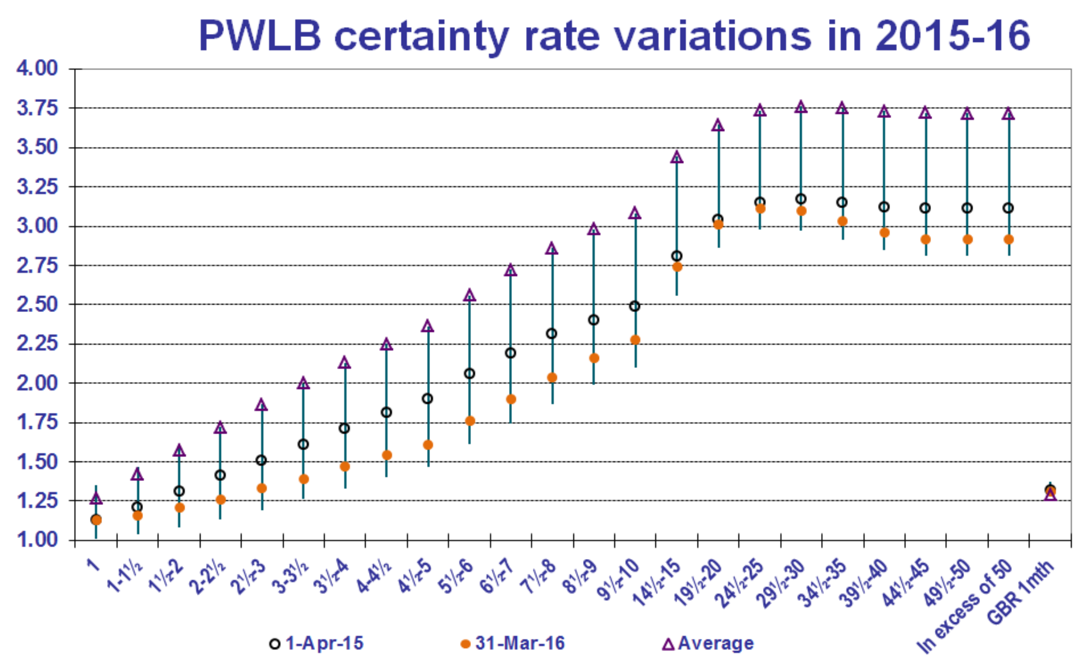
On the international scene, concerns have increased about the slowing of the Chinese economy and also its potential vulnerability to both the bursting of a property bubble and major exposure of its banking system to bad debts. The Japanese economy has also suffered disappointing growth in this financial year despite a huge programme of quantitative easing, while two of the major emerging market economies, Russia and Brazil, are in recession. The situations in Ukraine, and in the Middle East with ISIS, have also contributed to volatility.

The UK elected a majority Conservative Government in May 2015, removing one potential concern but introducing another due to the promise of a referendum on the UK remaining part of the EU. The government maintained its tight fiscal policy stance but the more recent downturn in expectations for economic growth has made it more difficult to return the public sector net borrowing to a balanced annual position within the period of this parliament.

6. Borrowing Rates in 2015/16

PWLB borrowing rates - the graphs and table for PWLB maturity rates below show, for a selection of maturity periods, the high and low points in rates, the average rates, spreads and individual rates at the start and the end of the financial year.





	1	1-1.5	2.5-3	3.5-4	4.5-5	9.5-10	24.5-25	49.5-50	1 month variable
1/4/15	1.130%	1.210%	1.510%	1.710%	1.900%	2.490%	3.150%	3.110%	1.320%
31/3/16	1.130%	1.160%	1.330%	1.470%	1.610%	2.280%	3.110%	2.920%	1.310%
High	1.350%	1.470%	1.860%	2.120%	2.350%	3.060%	3.660%	3.580%	1.370%
Low	1.010%	1.040%	1.190%	1.330%	1.470%	2.100%	2.980%	2.810%	1.310%
Average	1.212%	1.302%	1.608%	1.814%	2.004%	2.653%	3.348%	3.216%	1.336%
Spread	0.340%	0.430%	0.670%	0.790%	0.880%	0.960%	0.680%	0.770%	0.060%
High date	05/08/2015	06/08/2015	02/07/2015	15/07/2015	14/07/2015	14/07/2015	02/07/2015	14/07/2015	30/10/2015
Low date	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016	21/03/2016

Short-dated market money:- sourced from other UK public bodies, rates fluctuated throughout the year from 0.26%-0.60% for 1 to 12 month maturities.

7. Borrowing Outturn for 2015/16

New Treasury Borrowing:-

New loans were drawn to fund the net unfinanced capital expenditure and naturally maturing debt.

The loans drawn were:-

Table 9: New Loans Taken in Financial Year 2015/16						
Lender	**Date Taken**	**Principal £000's**	**Interest Rate**	**Fixed/ Variable**	**Maturity Date**	**Term (Yrs)**
PWLB	27 Aug 2015	£ 7,049	2.92%	Fixed	27 Aug 2062	47.00
Salix	02 Dec 2015	£ 200	0.00%	Fixed	01 Oct 2023	7.83
Market	Various	£213,020	0.26%-0.55%	Variable interest rate	Various	0.06-0.25
Total		**£220,269**				

Market loans of £173.5 million reflect an average carrying value of £26m of Temporary Borrowing drawn on average every 1.8 months. This compares against a budget assumption of new short-term market borrowing of £50.0 million at an average interest rate of 0.63%.

Medium-long term borrowing of £7.249 million compares with a budget assumption of new borrowing of £46.5 million at an average interest rate of 3.44%.

Maturing Debt:-

The following table gives details of treasury debt maturing during the year:-

Table 10: Maturing Debt in Financial Year 2015/16						
Lender	**Date Repaid**	**Principal £000's**	**Interest Rate**	**Fixed/ Variable**	**Date Originally Taken**	**Original Term (Yrs)**
PWLB	Various (Annuities)	£ 26	8.72%	Fixed	Various	59.75
PWLB	27 Aug 2015	£ 5,000	1.84%	Fixed	27 Aug 2010	5.00
Salix	1 Sep / 1 Mar	£ 36	0.00%	Fixed	02 Oct 2014	6.92
Market	Various	£212,640	0.26%-0.48%	Variable interest rate	Various	0.08-1.00
Total		**£217,702**				

Rescheduling:-

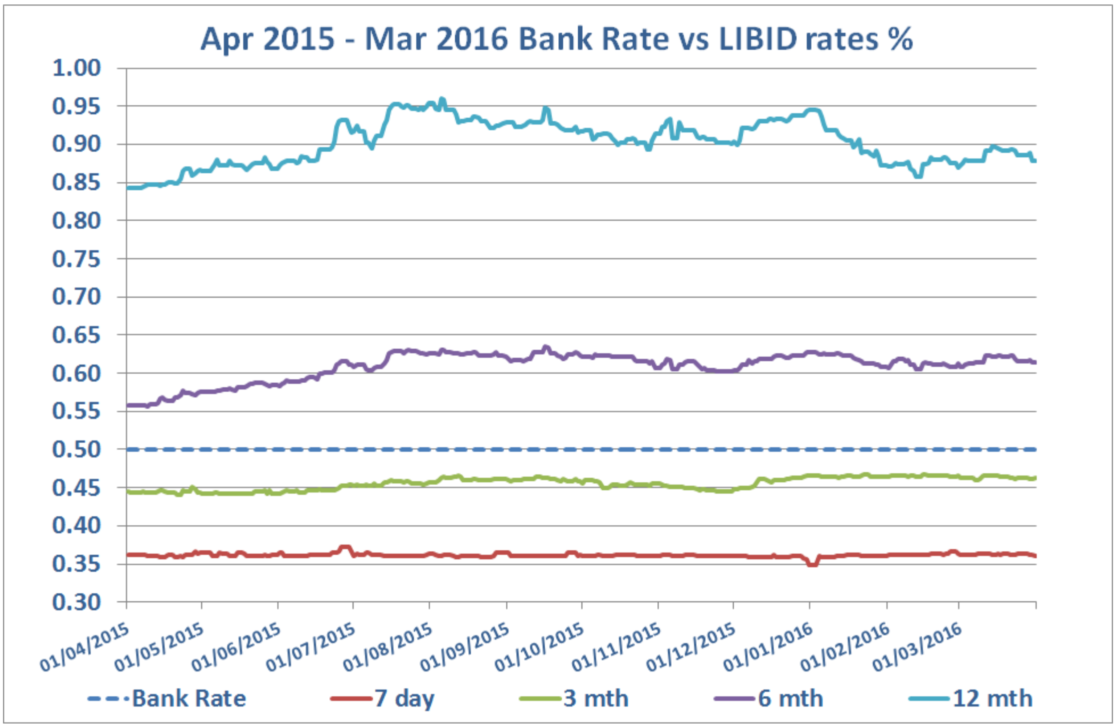
No rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

Summary of debt transactions:-

The average interest rate payable on external debt increased from 3.59% to 3.61%, as a result of the repayment of low coupon PWLB loans.

8. Investment Rates in 2015/16

Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for seven years. Market expectations as to the timing of the start of monetary tightening started the year at quarter 1 2016 but then moved back to around quarter 2 2018 by the end of the year. Deposit rates remained depressed during the whole of the year, primarily due to the effects of the Funding for Lending Scheme and due to the continuing weak expectations as to when Bank Rate would start rising.



Money market fund rates started the year between 0.35%-0.45% and remained broadly unchanged, creeping slightly north towards base rate level (0.50%) towards the end of the financial year.

New products were launched by Santander in the middle of the year, with the Council taking advantage of the 1.15% payable on the 180 day notice account. Fixed Term Deposits were placed with both Bank of Scotland and Royal Bank of Scotland in the latter half of the year, to allow the balance sheet reserves to be broadly cash backed in full.

9. Investment Outturn for 2015/16

Investment Policy:-

The Council's investment policy is governed by Scottish Government Investment Regulations, which have been implemented in the annual investment strategy approved by the Council on 17/02/2015. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

Investments held by the Council:-

The Council maintained an average balance of £59.7 million of internally managed funds. The internally managed funds earned an average rate of return of 0.79%. The comparable performance indicator is the average 6-month LIBID un-compounded rate, which was 0.61%. This compares with a budget assumption of £57.8 million of internally managed funds earning an average rate of 0.96%.

Summary of investment transactions:-

The challenging investment environment saw a reduction in the level of investment returns of £82,000 compared with budget (£474,000 interest return against a budgeted assumption of £556,000).

10. Performance Measurement

One of the key requirements in the Code is the formal introduction of performance measurement relating to investments, debt and capital financing activities.

Loans Fund Rate

Combining the interest paid (earned) on external debt (investments) with charges for premiums written off and internal interest allowed into an average Loans Fund Rate, Midlothian's result of 3.23% for 2014/15 was the second lowest Loans Fund Rate amongst all mainland authorities in Scotland (see Appendix 1).

The comparative Loans Fund Rate for 2015/16, of 3.28%, is once again expected to be one of the lowest when benchmarked against all mainland authorities in Scotland (note that at present, these benchmark figures are not yet available).

Investment Benchmarking

The Council participates in the Scottish Investment Benchmarking Group set up by its Treasury Management Consultants, Capita. This service provided by Capita provides benchmarking data to authorities for reporting and monitoring purposes, by measuring the security, liquidity and yield within an individual authority portfolio. Based on the Council's investments as at 31 March 2015, the Weighted Average Rate of Return (WARoR) on investments of 0.88% against other authorities is shown in the graph below:-

	Actual WARoR	Model WARoR	Difference	Lower Bound	Upper Bound	Performance
Midlothian Council	0.85%	0.59%	0.26%	0.53%	0.65%	Above

** Models for 30 June 2015, 30 September 2015 and 31 December 2015 are attached as Appendix 3.*

As can be seen from the above graph, Midlothian is performing above the Capita model benchmarks (red to green lines), and is achieving one of the highest Weighted Average Rates of Return (WARoR) for the Weighted Average Credit Risk held, not only amongst peer Councils within the Benchmarking Group but also amongst the population of authorities across the UK.

Debt Performance

Whilst investment performance criteria have been well developed and universally accepted, debt performance indicators continue to be a more problematic area with the traditional average portfolio rate of interest acting as the main guide. In this respect, the relevant figures for Midlothian are incorporated in the table in Section 3.

11. Conclusion

The Council's overall cost of borrowing continues to benefit from proactive Treasury Management activity.

The cost of long term borrowing has been maintained by taking up opportunities to borrow from the PWLB at low interest rates whilst advantage has also been taken of the low rates available for temporary borrowing.

A better than average return on investments has been achieved for the tenth consecutive year and Midlothian continues to perform above the Sector model benchmarks and is achieving one of the highest Weighted Average Rates of Return (WARoR) for the Weighted Average Credit Risk held, not only amongst peer Councils within the Benchmarking Group but also amongst the population of authorities across the UK.

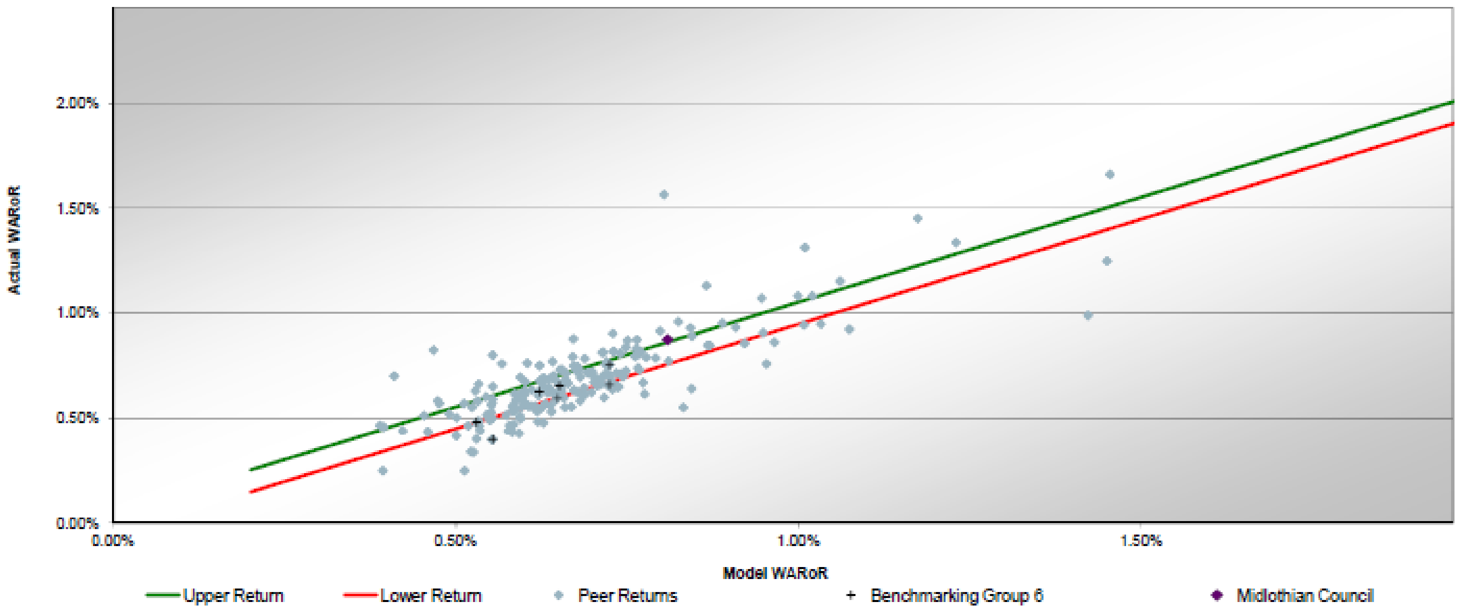
Overall Midlothian's Loans Fund Rate of 3.28% for the year is expected to be one of the lowest when benchmarked against all mainland Authorities in Scotland.

Appendix 3

Midlothian Council Investment Portfolio return as at 30 June 2015

Midlothian Council

Population Returns against Model Returns



	Actual WARoR	Model WARoR	Difference	Lower Bound	Upper Bound	Performance
Midlothian Council	0.87%	0.81%	0.07%	0.76%	0.86%	Above

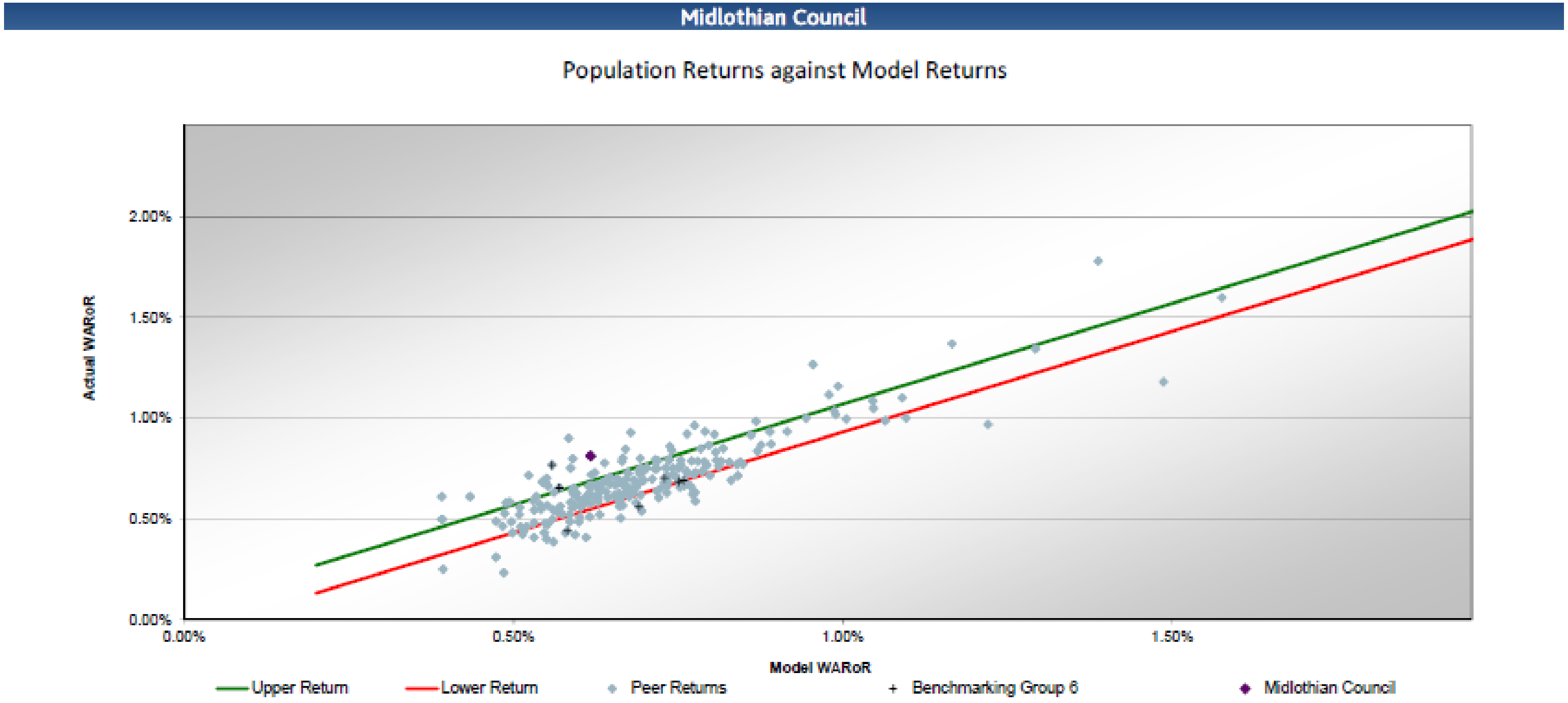
Midlothian Council Investment Portfolio return as at 30 September 2015

Midlothian Council

Population Returns against Model Returns

	Actual WARoR	Model WARoR	Difference	Lower Bound	Upper Bound	Performance
Midlothian Council	0.84%	0.85%	-0.01%	0.80%	0.90%	Inline

Midlothian Council Investment Portfolio return as at 31 December 2015



	Actual WARoR	Model WARoR	Difference	Lower Bound	Upper Bound	Performance
Midlothian Council	0.81%	0.62%	0.19%	0.55%	0.69%	Above