PCC
POLICE AND CRIME COMMISSIONER FOR ESSEX

PCC Decision Report

Report reference number: 0092/17 **Classification: Not Protectively Marked**
Title of report: Treasury Management Outturn Report 2016/17
Area of County/Stakeholders affected: Countywide
Report by : Treasurer **Date of report: 25th September 2017** **Enquiries to:** Charles Garbett: 01245 291603, charles.garbett@essex.police.uk; Matthew Tokley, matthew.tockley@essex.pnn.police.uk

1. Purpose

1.1 To present treasury management activities performed during 2016/17.

2. Recommendations

2.1 The PCC is recommended to note the treasury activities for 2016/17.

3. Background

3.1 The PCC complies with the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2011 Edition* (the CIPFA Code) which requires the PCC to approve a treasury management annual report after the end of each financial year. This report fulfils the PCC's legal obligation to have regard to the CIPFA Code.

3.2 The PCC's treasury management strategy for 2016/17 was approved by the PCC on 29th June 2016. The PCC has invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the PCC's treasury management strategy.

4. External Context

4.1 **Economic background:** Politically, 2016/17 was an extraordinary twelve month period which defied expectations when the UK voted to leave the European Union and Donald Trump was elected the 45th President of the USA. Uncertainty over the outcome of the US presidential election, the UK's future relationship with the EU and the slowdown witnessed in the Chinese economy in early 2016 all resulted in significant market volatility during the year. Article 50 of the Lisbon Treaty, which sets in motion the 2-year exit period from the EU, was triggered on 29th March 2017.

4.2 UK inflation had been subdued in the first half of 2016 as a consequence of weak global price pressures, past movements in sterling and restrained domestic price growth. However the sharp fall in the Sterling exchange rate following the referendum had an impact on import prices which, together with rising energy prices, resulted in CPI rising from 0.3% year/year in April 2016 to 2.3% year/year in March 2017.

4.3 In addition to the political fallout, the referendum's outcome also prompted a decline in household, business and investor sentiment. The repercussions on economic growth were judged by the Bank of England to be sufficiently severe to prompt its Monetary Policy Committee (MPC) to cut the Bank Rate to 0.25% in August and embark on further gilt and corporate bond purchases as well as provide cheap funding for banks via the Term Funding Scheme to maintain the supply of credit to the economy.

4.4 Despite growth forecasts being downgraded, economic activity was fairly buoyant and GDP grew 0.6%, 0.5% and 0.7% in the second, third and fourth calendar quarters of 2016. The labour market also proved resilient, with the ILO unemployment rate dropping to 4.7% in February, its lowest level in 11 years.

4.5 Following a strengthening labour market, in moves that were largely anticipated, the US Federal Reserve increased rates at its meetings in December 2016 and March 2017, taking the target range for official interest rates to between 0.75% and 1.00%.

4.6 **Financial markets:** Following the referendum result, gilt yields fell sharply across the maturity spectrum on the view that Bank Rate would remain extremely low for the foreseeable future. After September there was a reversal in longer-dated gilt yields which moved higher, largely due to the MPC revising its earlier forecast that Bank Rate would be dropping to near 0% by the end of 2016. The yield on the 10-year gilt rose from 0.75% at the end of September to 1.24% at the end of December, almost back at pre-referendum levels of 1.37% on 23rd June. 20- and 50-year gilt yields also rose in Q3 2017 to 1.76% and 1.70% respectively, however in Q4 yields remained flat at around 1.62% and 1.58% respectively.

4.7 After recovering from an initial sharp drop in Q2, equity markets rallied, although displaying some volatility at the beginning of November following the US presidential election result. The FTSE-100 and FTSE All Share indices closed at 7342 and 3996 respectively on 31st March, both up 18% over the year. Commercial property values fell around 5% after the referendum, but had mostly recovered by the end of March.

4.8 Money market rates for overnight and one week periods remained low since Bank Rate was cut in August. 1- and 3-month LIBID rates averaged 0.36% and 0.47% respectively during 2016-17. Rates for 6- and 12-months increased between August and November, only to gradually fall back to August levels in March, they averaged 0.6% and 0.79% respectively during 2016-17.

4.9 **Credit background:** Various indicators of credit risk reacted negatively to the result of the referendum on the UK's membership of the European Union. UK bank credit default swaps saw a modest rise but bank share prices fell sharply, on average by 20%, with UK-focused banks experiencing the largest falls. Non-UK bank share prices were not immune, although the fall in their share prices was less pronounced.

4.10 Fitch and Standard & Poor's downgraded the UK's sovereign rating to AA. Fitch, S&P and Moody's have a negative outlook on the UK. Moody's has a negative outlook on those banks and building societies that it perceives to be exposed to a more challenging operating environment arising from the 'leave' outcome.

4.11 None of the banks on the PCC's lending list failed the stress tests conducted by the European Banking Authority in July and by the Bank of England in November, the latter being designed with more challenging stress scenarios, although Royal Bank of Scotland was one of the weaker banks in both tests. The tests were based on banks' financials as at 31st December 2015, 11 months out of date for most. As part of its creditworthiness research and advice, the PCC's treasury advisor Arlingclose regularly undertakes analysis of relevant ratios - "total loss absorbing capacity" (TLAC) or "minimum requirement for eligible liabilities" (MREL) - to determine whether there would be a bail-in of senior investors, such as local authority unsecured investments, in a stressed scenario.

5. Local Context

5.1 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These factors and the year-on-year change are summarised in table 1 below.

Table 1:

Investments	**1st April 2016**	**31st March 2017**
	£000	**£000**
Fixed Term Deposits	-	11,500
Call Accounts	18,159	3,000
Total	18,159	14,500

5.2 Call accounts are used for depositing and withdrawing liquid funds on a day-to-day basis. There are two call accounts, with Barclays and Santander UK. The Barclays account was used throughout the year and the Santander account has been used since January 2014.

5.3 Fixed term deposits are used for investing the PCC's core funds, i.e. the cash backed element of reserves that is not required on a day-to-day basis. Investment activity during the year has been undertaken with the Bank of England Debt Management Office and with UK financial institutions such as Lloyds and Nationwide Building Society.

5.4 No other investment instruments have been used during the year.

5.5 The average level of investments during the year was £23.446m compared to £26.768m in 2015/16. Interest earnings for the year were £78k, representing an average return of 0.33% a decrease on 2015/16 where the average return was 0.50%. The budgeted investment income for the year was £0. No income target was set for 2016/17 as Essex Police had budgeted to be in a borrowing position in 2015/16. At the time this was due to the significant estates capital investment programme which included a new force headquarters.

Borrowings

5.6 There were no long term borrowings during 2016/17.

Compliance with Treasury Management Strategy

5.7 The Treasurer is pleased to report that all treasury management activities undertaken during 2016/17 complied fully with the CIPFA Code of Practice and the Authority's approved Treasury Management Strategy. Compliance with specific investment limits is demonstrated below in table 2.

Table 2:

	2016/17 £m	Complied
Upper limit on fixed interest rate exposure	15	✓
Upper limit on variable interest rate exposure	15	✓
Limit on principle invested beyond year end or over 364 days	0	✓
Operational Borrowing (estimate)	15	✓
Authorised limit for external borrowing (estimate)	17	✓

5.8 Interest rate exposure: This indicator is set to control the PCC's exposure to interest rate risk for borrowing.

5.9 No funds will be invested beyond 364 days: the purpose of this indicator is to control the PCC's exposure to the risk of incurring losses by seeking early repayment of its investments.

5.10 Operational boundary: This term refers to the limit of total debt which the PCC would not normally expect to exceed. The borrowing figures are based on the approved capital programme for the year.

5.11 Authorised limit for external borrowing: this is the limit that the PCC is required to set for total external borrowing, including short-term borrowing.

6. Police and Crime Plan

6.1 Not applicable

7. Police Operational Implications

7.1 Not applicable

8. Financial Implications

8.1 Detailed within the report.

9. Legal Implications

9.1 Approval of the Treasury Management Strategy satisfies the requirements of the Local Government Act 2003, CIPFA Prudential Code, CLG MRP Guidance, CIPFA Treasury Management Code & CLG Investment Guidance

10. Staffing and other resource implications

10.1 Not applicable

11. Equality and Diversity implications

11.1 Not applicable

12. Background papers

Report Approval

The report will be signed off by the OPCC Chief Executive and Treasurer, prior to review and sign off by the PCC / DPCC .

Chief Executive/M.O Sign: ....

Print: S. Haye ....

Chief Financial Officer/Treasurer Sign: ....

Print: CHARLES L GARRETT ....

Publication

Is the report for publication? **YES** ☐

NO ☐

If 'NO', please give reasons for non-publication *(state 'None' if applicable)*

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If the report is not for publication, the Chief Executive will decide if and how the public can be informed of the decision.

Redaction

If the report is for publication, is redaction required:

1. Of Decision Sheet	**YES**	☐	**2. Of Appendix**	**YES**	☐
	NO	☑		**NO**	☑

If 'YES', please provide details of required redaction:

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Date redaction carried out: ....

Treasurer / Chief Executive Sign Off – for Redactions only

If redaction is required, Treasurer or Chief Executive are to sign off that redaction has been completed.

Sign: ....

Print: ....

Chief Executive/Treasurer

Date signed: ....

Please continue to next page for Final PCC Decision and Final Sign Off

Decision and Final Sign Off

I agree the recommendations to this report;

Sign: ....

Print: R. C. Hirst ....

PCC/~~Deputy PCC~~

Date signed: 9/10/17 ....

I do not agree the recommendations to this report because;

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Sign: ....

Print: ....

PCC/Deputy PCC

Date signed: ....