

<b>ISLE OF ANGLESEY COUNTY COUNCIL</b>	
<b>REPORT TO:</b>	<b>COUNTY COUNCIL</b>
<b>DATE:</b>	<b>27 SEPTEMBER 2016</b>
<b>SUBJECT:</b>	<b>ANNUAL TREASURY MANAGEMENT REVIEW FOR 2015/16</b>
<b>PORTFOLIO HOLDER(S):</b>	<b>COUNCILLOR H E JONES</b>
<b>LEAD OFFICER(S):</b>	<b>R MARC JONES</b>
<b>CONTACT OFFICER(S):</b>	<b>CLAIRE KLIMASZEWSKI/ELFED ROBERTS (EXT. 1865/2608)</b>
<b>Nature and reason for reporting</b>	
<p>To comply with regulations issued under the Local Government Act 2003 and with the Council's Treasury Management Scheme of Delegation for 2015/16 (Appendix 8 of the Treasury Management Strategy Statement 2015/16). In accordance with the Scheme of Delegation, this report was scrutinised by the Audit Committee on 25 July 2016, and the Committee resolved to accept and note this report, and to forward it to the Executive without further comment. The report was accepted by the Executive on 19 September 2016 and passed to the County Council without further comment.</p>	

## Summary

The Council is required by regulations issued under the Local Government 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 (received on 26 February 2015);
- a mid-year treasury update report (received on 10 March 2016);
- an annual review following 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 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.

In order to support the scrutiny role of the members of the Audit Committee Member training on treasury management issues was undertaken during July 2014 and a refresher course will be provided during 2016.

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

Data for actual prudential and treasury indicators	2014/15 Actual £000	2015/16 Original £000	2015/16 Actual £000
Capital expenditure			
• Non-HRA	15,769	15,520	16,369
• HRA	5,518	8,590	27,607
• Total	21,287	24,110	43,976
Total Capital Financing Requirement:			
• Non-HRA	85,926	92,787	84,297
• HRA	22,650	43,836	43,360
• Total	108,576	136,623	127,657
Gross borrowing	89,590	126,000	110,744
External debt	89,590	165,000	110,744
Investments			
• Longer than 1 year			-
• Under 1 year	10,983		16,210
• Total	10,983		16,210

Other prudential and treasury indicators are to be found in the main body of this report. The S151 Officer also confirms that borrowing was only undertaken for a capital purpose and the statutory borrowing limit (the authorised limit), was not breached.

The financial year 2015/16 continued the challenging investment environment of previous years, namely low investment returns.

## RECOMMENDATIONS

The Committee is recommended to:-

- (i) Note that the outturn figures in this report will remain provisional until the audit of the 2015/16 Statement of Accounts is completed and signed off; any resulting significant adjustments to the figures included in this report will be reported as appropriate;
- (ii) Note the provisional 2015/16 prudential and treasury indicators in this report;
- (iii) Consider the annual treasury management report for 2015/16 and pass on to the next meeting of the Executive with any comments.

## Appendices:

- Appendix 1 - Summary Portfolio Valuation as at 31 March 2016
- Appendix 2 - Credit ratings of investment counterparties and deposits held with each as at 31 March 2016
- Appendix 3 - Credit ratings of investment counterparties and deposits held with each at 15 July 2016
- Appendix 4 - The Economy and Interest Rates – A Commentary by Capita Asset Services

## Background papers

- Treasury Management Strategy Statement 2015/16
- Prudential and Treasury Indicators 2015/16
- Treasury Management Mid-Year Review Report 2015/16

## 1. INTRODUCTION

This report summarises the following functions / activities / outcomes in financial year 2015/16:-

- Capital activity;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- The actual prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity.

## 2. THE COUNCIL'S CAPITAL EXPENDITURE AND FINANCING 2015/16

**2.1** 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
- Financed from borrowing; this may be through planned borrowing or otherwise. If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

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

£m	2014/15 Actual (£m)	2015/16 Estimate (£m)	2015/16 Actual (£m)
Non-HRA capital expenditure	16	15	16
HRA capital expenditure	5	9	28
<b>Total capital expenditure</b>	<b>21</b>	<b>24</b>	<b>44</b>
Non-HRA financed in year	11	8	18
HRA financed in year	5	6	3
<b>Non-HRA capital expenditure financed by borrowing</b>	<b>5</b>	<b>10</b>	<b>2</b>
<b>HRA capital expenditure financed by borrowing</b>	<b>0</b>	<b>0</b>	<b>21</b>

## 3. THE COUNCIL'S OVERALL BORROWING NEED

**3.1** 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 debt position. 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 capital expenditure financed by borrowing (see above table), and prior years' capital expenditure funded by borrowing which has not yet been paid for by revenue or other resources.

**3.2** 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.

### 3.3 Reducing the CFR

**3.3.1** 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 Minimum Revenue Provision – MRP, 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.

**3.3.2** 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 statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

**3.3.3** The Council's 2015/16 MRP Policy (as required by WG Guidance) was approved as part of the Treasury Management Strategy Report for 2015/16 on 26 February 2015.

**3.3.4** The Council's CFR for the year is shown below, and represents a key prudential indicator. This would include any PFI and leasing schemes on the balance sheet, which would increase the Council's borrowing need, the CFR. There were no such schemes during the year.

CFR: Council Fund	2014/ 15 Actual (£m)	2015/ 16 Budget (£m)	2015/ 16 Actual (£m)
Opening balance	85	93	86
Add capital expenditure financed by borrowing(as above)	5		2
Less MRP/VRP*	(4)	(4)	(4)
Closing balance	86	92	84

CFR: HRA	2014/ 15 Actual (£m)	2015/ 16 Budget (£m)	2014/ 15 Actual (£m)
Opening balance	24	44	23
Add unfinanced capital expenditure (as above)	-	-	21
Less MRP/VRP*	(1)	(1)	(1)
Closing balance	23	43	43

\* Includes voluntary application of capital receipts

**3.3.5** The borrowing activity is constrained by prudential indicators for gross borrowing and the CFR, and by the authorised limit.

### 3.4 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 plus the estimates of any additional capital financing requirement for the current 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. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	31 March 2015 Actual (£m)	31 March 2016 Budget (£m)	31 March 2016 Actual (£m)
Gross borrowing position	89.6	110.7	110.7
CFR	108.6	136.6	127.7

**3.4.1** As part of the financing of capital expenditure for 2015/16 borrowing was used to finance the gap between available resources (capital receipts, capital grants, capital contributions and revenue contributions) and the capital expenditure. It was decided, in light of current and projected market interest rates and counterparty credit risks, to continue internalising borrowing, in the short term at least. This means that instead of borrowing externally from the PWLB, the Council has instead used its own council reserves. This strategy has now been implemented throughout each of the last five years. As a result of continuing with this strategy, the gap between CFR and external borrowing increased during 2015/16 by £19m. The gross borrowing at 31 March 2016 is less than the forecast CFR for the following 2 years. The gross borrowing position has increased during 2015/16 due to the loan from the PWLB for the HRA Buy-out which replaces the former subsidy payments to Welsh Government. This has also had a significant impact on the capital financing requirement.

**3.5** The other debt related indicators are:

**3.5.1 The authorised limit** - the authorised limit is the "affordable borrowing limit" required by section 3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2015/16 the Council maintained gross borrowing within its authorised limit.

**3.5.2 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 are acceptable subject to the authorised limit not being breached.

**3.5.3 Actual financing costs as a proportion of net revenue stream** - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2015/16
Authorised limit	£165.0m
Maximum gross borrowing position	£110.7m
Operational boundary	£126.0m
Average gross borrowing position	£110.7m
Financing costs as a proportion of net revenue stream - CF	6.06%
Financing costs as a proportion of net revenue stream - HRA	13.83%

The reason for the Council Fund financing costs being a marginally lower percentage of the net revenue stream than estimated in the Treasury Management Strategy 2015/16 (6.53%) was due to lower than budgeted financing costs, combined with lower than budgeted investment income and higher than expected net revenue stream.

#### 4. TREASURY POSITION AS AT 31 MARCH 2016

4.1 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 summary, and through officer activity in accordance with the Treasury Management Strategy 2015/16. The borrowing and investment figures for the Council as at the end of the 2014/15 and 2015/16 financial years are as follows:-

	31 MARCH 2015			31 MARCH 2016		
	£'000	Average Rate (%)	Average Maturity (yrs)	£'000	Average Rate (%)	Average Maturity (yrs)
Debt: All Public Works Loans Board, fixed rate	89,585	5.72	25.4	110,741	5.72	24.9
CFR	108,582			127,657		
Over / (under) borrowed	(18,997)			(16,916)		
Fixed term investments (all < 1 year, managed in house and fixed rate)	Nil			5,000	0.50	
No notice investments (all managed in house)	10,983	0.36		11,209	0.35	
Total Investments	10,983	0.36		16,209	0.40	

See a more detailed analysis in Appendix 1. The upper limits for fixed rate and variable rate exposures were not breached during the year.

4.2 Borrowing is further broken down by maturity as:-

	31 MARCH 2015		31 MARCH 2016		2014/15 and 2015/16 Limits	
	£m	% of total	£m	% of total	% of total (upper)	% of total (lower)
Total borrowing	89.6	100	110.7	100		
Under 12 months	0.0	0.0	0.0	0.0	20	0
12 months and within 24 months	0.0	0.0	5.5	4.97	20	0
24 months and within 5 years	15.5	17.3	14.5	13.10	50	0
5 years and within 10 years	8.8	9.8	4.2	3.79	75	0
10 years and above	65.3	72.9	86.5	78.14	100	0

4.3 There was no debt rescheduling during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable. New external borrowing of £21.169m was taken out during the year to fund the HRA Buy-out from the Welsh Government HRA Subsidy system.

- 4.4 Part of the Council's deposits are held in no notice deposit accounts which pay interest at rates near the prevailing base rate, £11.0m at 0.35% (31 March 2015 11m at 0.36%). There was one deposit being held for a period of less than 1 year for £5m at an interest rate of 0.50% (31 March 2015: Nil).

## 5. TREASURY STRATEGY FOR 2015/16

- 5.1 The expectation for interest rates within the strategy for 2015/16 anticipated low but rising Bank Rate (starting in quarter 1 of 2015), and gradual rises in medium and longer term fixed borrowing rates during 2015/16. 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.
- 5.2 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.
- 5.3 The actual movement in gilt yields meant that PWLB rates saw little overall change during the first four months of the year but there was then a downward trend for the rest of the year with a partial reversal during February.
- 5.4 The economic position and PWLB and investment rates are shown in Appendix 4.

## 6. INVESTMENT OUTTURN FOR 2015/16

- 6.1 The 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.
- 6.2 The expected investment strategy was to keep to shorter term deposits (up to 364 days) although the ability to invest out to longer periods was retained. Available cash balances were expected to be up to £30m, ranging between £15m and £35m. The budget was set at 0.75% or £225k after adjusting for the higher rates on existing investments. As it turned out, average balances of £20.4m returned £88k (0.36%). The lower than budgeted average cash balance was partly the result of continuing to internalise borrowing. The lower than budgeted return was due to worse than anticipated rates of return on investments, with rates continuing to fall throughout the year.

## 7. INVESTMENT SECURITY AND CREDIT QUALITY

- 7.1 No institutions in which we had made investments had any difficulty in repaying investments and interest on time and in full during the year.

- 7.2** During 2015/16, credit ratings remained poor across the range of our usual counterparties. Since late 2008 it has been challenging to place deposits with appropriate counterparties. In December 2008, the Council's approval was obtained to extend flexibility with counterparties to deal with market changes; this included the ability to invest all our surplus funds with central government if necessary. The list was further widened in April 2010 to include nationalised and partly nationalised institutions and this list was clarified in March 2013 in relation to nationalised and part nationalised UK banks for the 2014/15 criteria. Previous decisions had extended flexibility for investing with local authorities. Appendix 2 shows the institutions where the Council's deposits were held as at 31 March 2016 and their ratings.
- 7.3** The practical effect of these policies was as follows: during the year we continued to use no notice accounts with major high street institutions (Santander, HSBC, RBS and Bank of Scotland) for day to day cash flow. In addition £5m was placed in 3 month deposits with Nationwide at a higher rate of 0.50%.

## **8. ACTIVITY DURING 2015/16**

- 8.1** It has previously been reported that this Authority was preparing to exit the HRA subsidy system on 2nd April 2015. At the time of reporting for Quarter 3 2014/15, treasury activity, it was known that the buyout was to be financed through the PWLB, but the settlement amount and rate of interest on the borrowing were under consultation. The potential effect of the buy-out was reflected in the budget setting papers presented to Members for 2015/16 (including the 2015/16 Treasury Management Strategy Statement presented to this Committee for scrutiny on 9th February 2015). It can be confirmed that that buy-out took place and the HRA is now self-financed. The exact structure of loans arranged by the Council to fund its self-financing of the HRA, reflected the requirements of the HRA business plan, the overall requirements of the Council and certain limitations, (e.g. the minimum average duration of any borrowing), put in place by the Welsh Government. The loans were, therefore, arranged at a set of bespoke, higher PWLB interest rates that applied only to Welsh HRA self-financing authorities and may make these loans less flexible, from a restructuring perspective, than would normally be the case.

## **9. ACTIVITY SINCE 2015/16**

- 9.1** The UK referendum result on 23 June 2016 to leave the European Union and the political instability which followed the result has created an economic shock which saw the value of sterling decrease; impacted on stock market values and led to UK banks long-term outlook being downgraded from stable outlook to negative outlook. All the council's deposits are held in banks which have been downgraded. However their short and medium term ratings are still within the appropriate ratings approved in the Treasury Management Strategy 2015/16. The status of the banks and the Council's deposits are under constant review to ensure that the Council's risks are minimised. The bank base rate has been held at the same rate currently at 0.50% however it is predicted that there will be a cut in the rate in the future to support the economy during the uncertain period following the EU referendum. While this would undermine interest earned on deposits further it would reduce the cost of borrowing from PWLB which would make external borrowing for capital expenditure more attractive. Appendix 3 shows the Council's current deposits and the ratings of the financial institutions the deposits are invested in (as at 15 July 2016). It shows that despite the downgrading of UK banks generally since the referendum there is little change in the individual ratings per institution the authority holds deposits in.



## **10. CONCLUSION**

- 10.1** A review of the Treasury Management Performance for 2015/16 has been provided. The year was fairly stable with the most significant activity being a loan from PWLB amounting to £21.169m for the HRA Buy-out from the annual subsidy to Welsh Government. This will not only save the Council money but offers the HRA increased flexibility to manage its housing stock. The council held appropriate cash balances at all times though the low interest rate meant that the returns were low. However this is consistent with the Treasury Management Strategy 2015/16 where the key objectives were low risk and ensuring there is sufficient cash to pay the council's creditors, etc. The financial position of the Council's financial instruments as at 31 March 2016 is shown in appendix 1.

**R MARC JONES  
HEAD OF FUNCTION (RESOURCES) &  
SECTION 151 OFFICER**

**25 JULY 2016**

**Summary Portfolio Valuation  
As at 31 March 2016**

<b>FINANCIAL ASSETS</b>	<b>Nominal / Principal (£)</b>	<b>Fair Value (£)</b>
Cash (interest bearing accounts) (1)	11,209,812	11,239,940
Fixed Term Deposits (2)	5,000,000	5,004,184
<b>FINANCIAL LIABILITIES</b>		
PWLB loan – Maturity	110,484,478	181,198,276
PWLB loan – Annuity	347,664	450,712
<b>Counterparties</b>		
<b>(1)</b> Cash (interest bearing accounts)		
Santander	6,783,222	
Bank of Scotland	707,475	
HSBC	3,718,240	
RBS	<u>875</u>	
	11,209,812	
<b>(2)</b> Fixed Term Deposits		
Nationwide Building Society	5,000,000	

ATODIAD / APPENDIX 2

Graddfeydd Credyd Gwrthbartion buddsoddi a'r adneuron a ddelir gyda phob un ar 31 Marwth 2016 \*  
Credit ratings of investment counterparties and deposits held with each as at 31 March 2016\*

Grŵp Bancio/ Banking Group	Sefydliad/ Institution	Adneuron / Deposit £'000	Hyd (Galw tymor sefydlog) / Duration (Call / Fixed Term**)	Cyfnod (O/I)/ Period (From - To)	Graddfa Dychweliad/ Rate of Return %	Graddfa Tymor Hir Fitch Long Term Rating ***	Graddfa Tymor Byr Fitch Short Term Rating ***	Graddfa Tymor Hir Moody's Long Term Rating ***	Graddfa Tymor Byr Moody's Short Term Rating ***	Graddfa Tymor Hir Standard & Poor's (S&P) Long Term Rating ***	Graddfa Tymor Byr Standard & Poor's (S&P) Short Term Rating ***	Lliw Sector/Hyd Awgrymiedig/ Sector Colour / Suggested Duration
Lloyds Banking Group plc	Bank of Scotland plc	707	Galw/ Call	n/a	0.40	A+	F1	A1	P-1	A	A-1	Coch – 6 mis/ Red - 6 months
HSBC Holdings plc	HSBC Bank plc	3,718	Galw/ Call	n/a	0.25	AA-	F1+	Aa2	P-1	AA-	A-1+	Oren – 12 mis / Orange – 12months
Santander Group plc	Santander UK plc	6,783	Galw/ Call	n/a	0.40	A	F1	A1	P-1	A	A-1	Coch - 6 mis / Red – 6 months
The Royal Bank of Scotland Group plc	The Royal Bank of Scotland plc	1	Galw/ Call	n/a	0.25	BBB+	F2	Ba1	NP	BBB-	A-3	
Not Applicable	Nationwide Building Society	5,000	Three month deposit		0.50	A	F1	A1	P-1	A	A-3	Coch – 6 Mis/Red 6 Months

\* Ceir y Rhestr Meini Prawf Gwrthbartion yn Atodiad 6 o'r Datganiad Strategaeth Rheoli Trysorlys 2015/16 / The Counterpart Criteria can be found at Appendix 6 of the 2015/16 Treasury Management Strategy Statement.

\*\* Sef tymor ar pwynt y buddsoddi/Being term at the point of investment.

ATODIAD / APPENDIX 3

Graddfeydd Credyd Gwrthbartion buddsoddi a'r adneuron a ddelir gyda phob un ar 15 Gorffennaf 2016 \*  
Credit ratings of investment counterparties and deposits held with each as at 15 July 2016\*

Grŵp Bancio/ Banking Group	Sefydliad/ Institution	Adneuron / Deposit £'000	Hyd (Galw tymor sefydlog) / Duration (Call / Fixed Term**)	Cyfnod (O/I)/ Period (From - To)	Graddfa Dychweliad/ Rate of Return %	Graddfa Tymor Hir Fitch Long Term Rating ***	Graddfa Tymor Byr Fitch Short Term Rating ***	Graddfa Tymor Hir Moody's Long Term Rating ***	Graddfa Tymor Byr Moody's Short Term Rating ***	Graddfa Tymor Hir Standard & Poor's (S&P) Long Term Rating ***	Graddfa Tymor Byr Standard & Poor's (S&P) Short Term Rating ***	Lliw Sector/Hyd Awgrymiedig/ Sector Colour / Suggested Duration
UK	N/A					AA	N/A	Aa1	N/A	AA	N/A	N/A
Lloyds Banking Group plc	Bank of Scotland plc	7,411	Galw/ Call	n/a	0.40	A+	F1	A1	P-1	A	A-1	Coch – 6 mis/ Red - 6 months
HSBC Holdings plc	HSBC Bank plc	2,423	Galw/ Call	n/a	0.25	AA-	F1+	Aa2	P-1	AA-	A-1+	Oren – 12 mis / Orange – 12months
Santander Group plc	Santander UK plc	7,499	Galw/ Call	n/a	0.40	A	F1	A1	P-1	A	A-1	Coch - 6 mis / Red – 6 months
The Royal Bank of Scotland Group plc	The Royal Bank of Scotland plc	2	Galw/ Call	n/a	0.25	BBB+	F2	Ba1	NP	BBB-	A-3	
Not Applicable	Nationwide Building Society	5,000	Three month deposit		0.50	A	F1	Aa3	P-1	A	A-1	Coch – 6 Mis/Red 6 Months
Total Deposits 15/07/16		22,736										

\* Ceir y Rhestr Meini Prawf Gwrthbartion yn Atodiad 6 o'r Datganiad Strategaeth Rheoli Trysorlys 2015/16 / The Counterpart Criteria can be found at Appendix 6 of the 2015/16 Treasury Management Strategy Statement.

\*\* Sef tymor ar pwynt y buddsoddi/Being term at the point of investment.

## 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 2016 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.

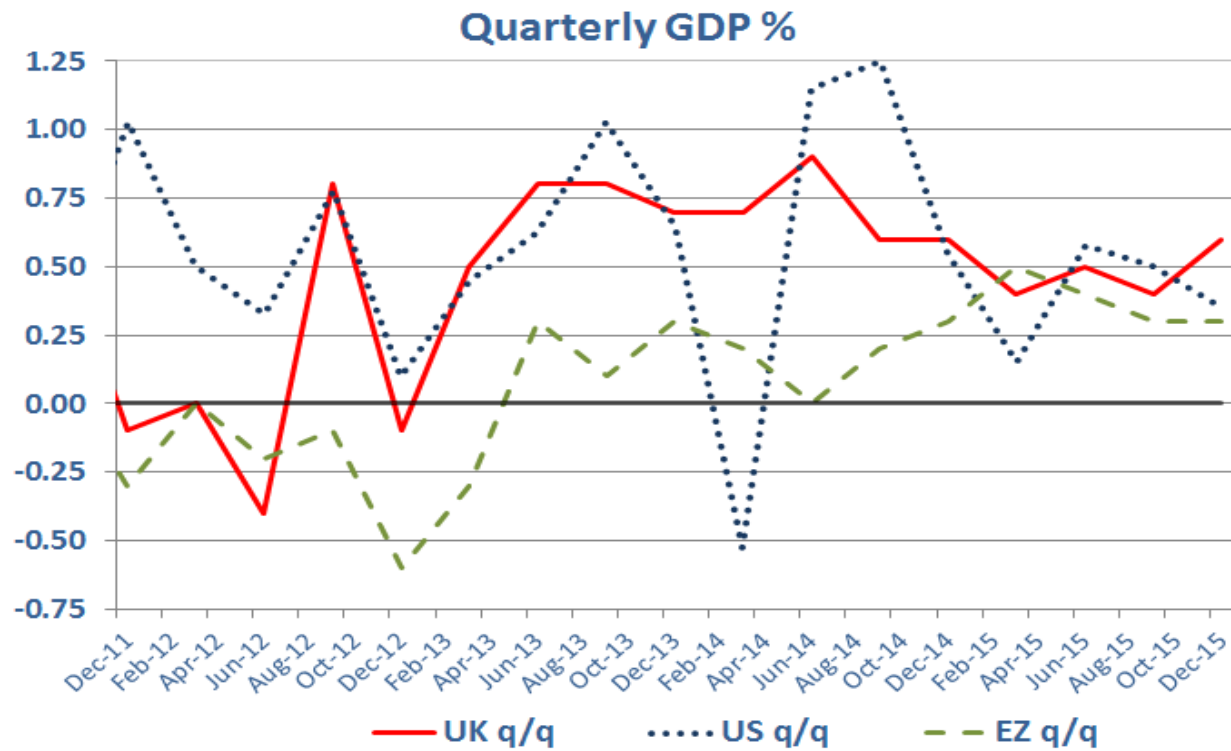
The ECB had announced in January 2015 that it would undertake a full blown quantitative easing programme of purchases of Eurozone government and other bonds starting in March at €60bn per month. This put downward pressure on Eurozone bond yields. There was a further increase in this programme of QE in 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.

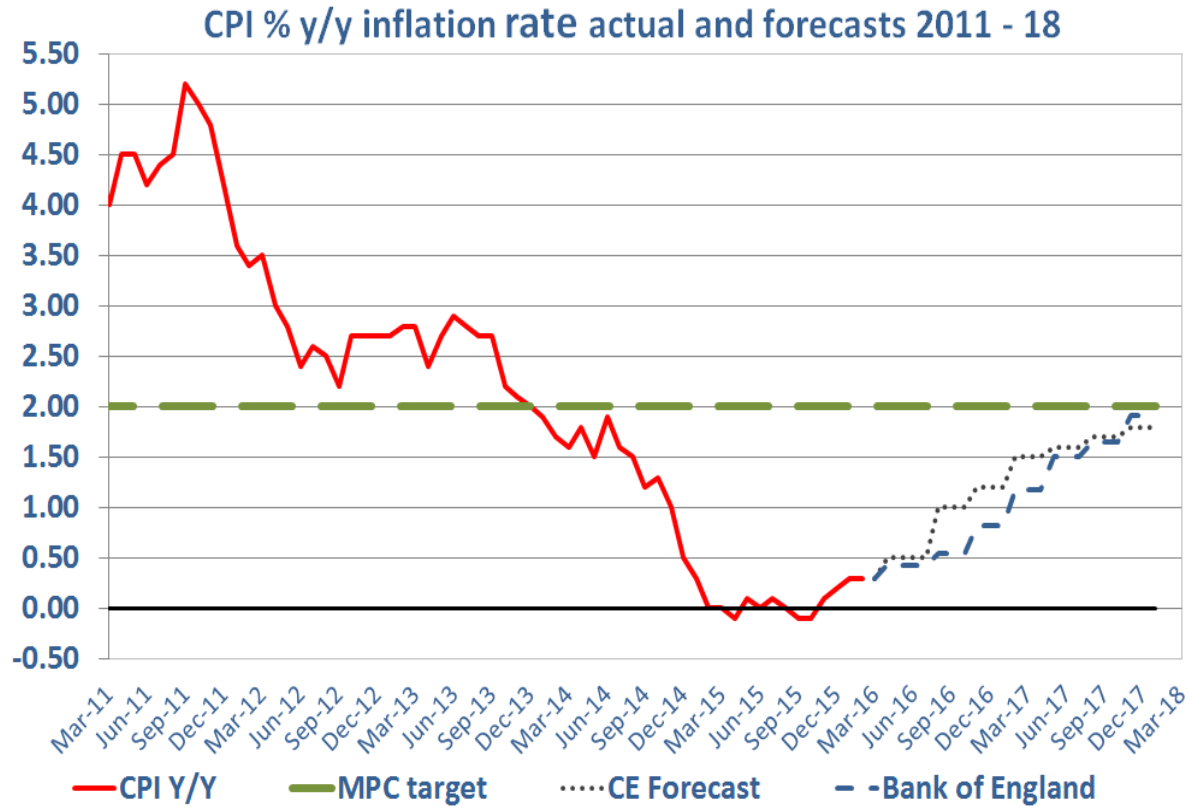
On the international scene, concerns have increased about the slowing of the Chinese economy and also its potential vulnerability to both the bursting of a property bubble and major exposure of its banking system to bad debts. The Japanese economy has also suffered disappointing growth in this financial 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.

### Gross Domestic Product Analysis (GDP)

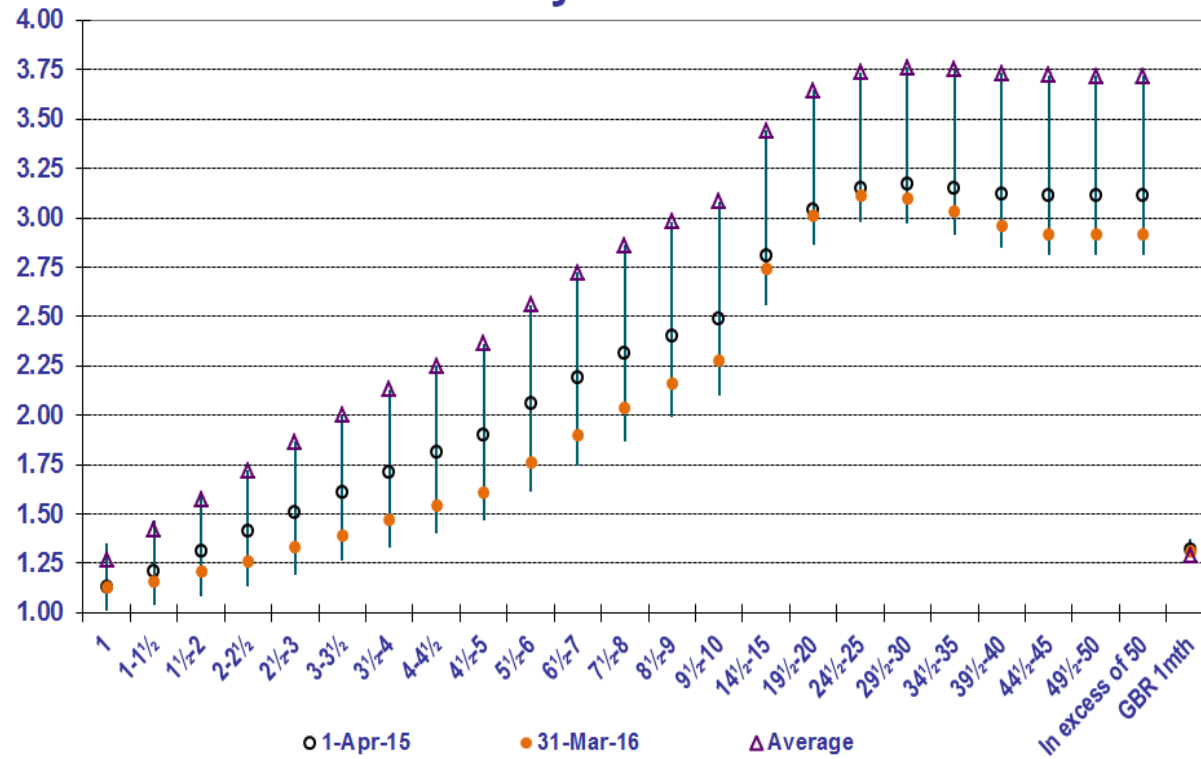


Inflation Rate Forecasts



**Public Works Loans Board Rates 2015-16**

### PWLB certainty rate variations in 2015-16

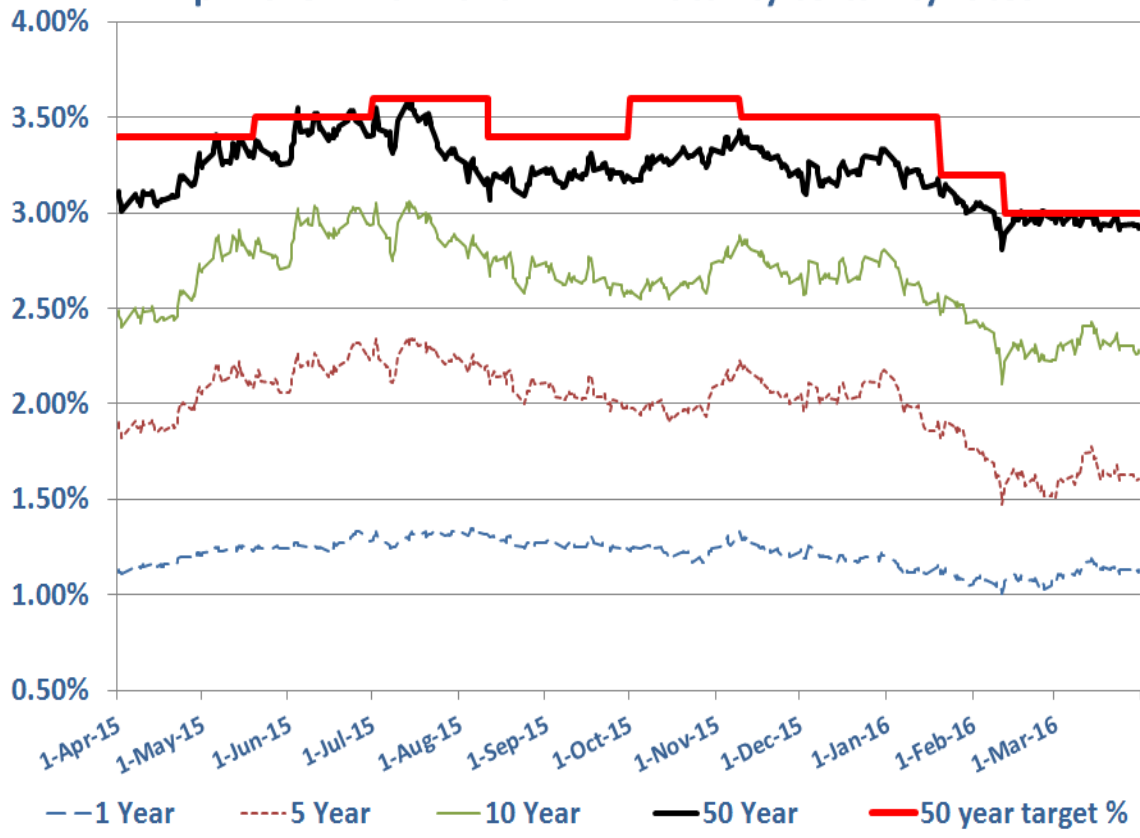




	1	1-1.5	2.5-3	3.5-4	4.5-5	9.5-10	24.5-25	49.5-50	1 month variable
1/4/15	1.130%	1.210%	1.510%	1.710%	1.900%	2.490%	3.150%	3.110%	1.320%
31/3/16	1.130%	1.160%	1.330%	1.470%	1.610%	2.280%	3.110%	2.920%	1.310%
High	1.350%	1.470%	1.860%	2.120%	2.350%	3.060%	3.660%	3.580%	1.370%
Low	1.010%	1.040%	1.190%	1.330%	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

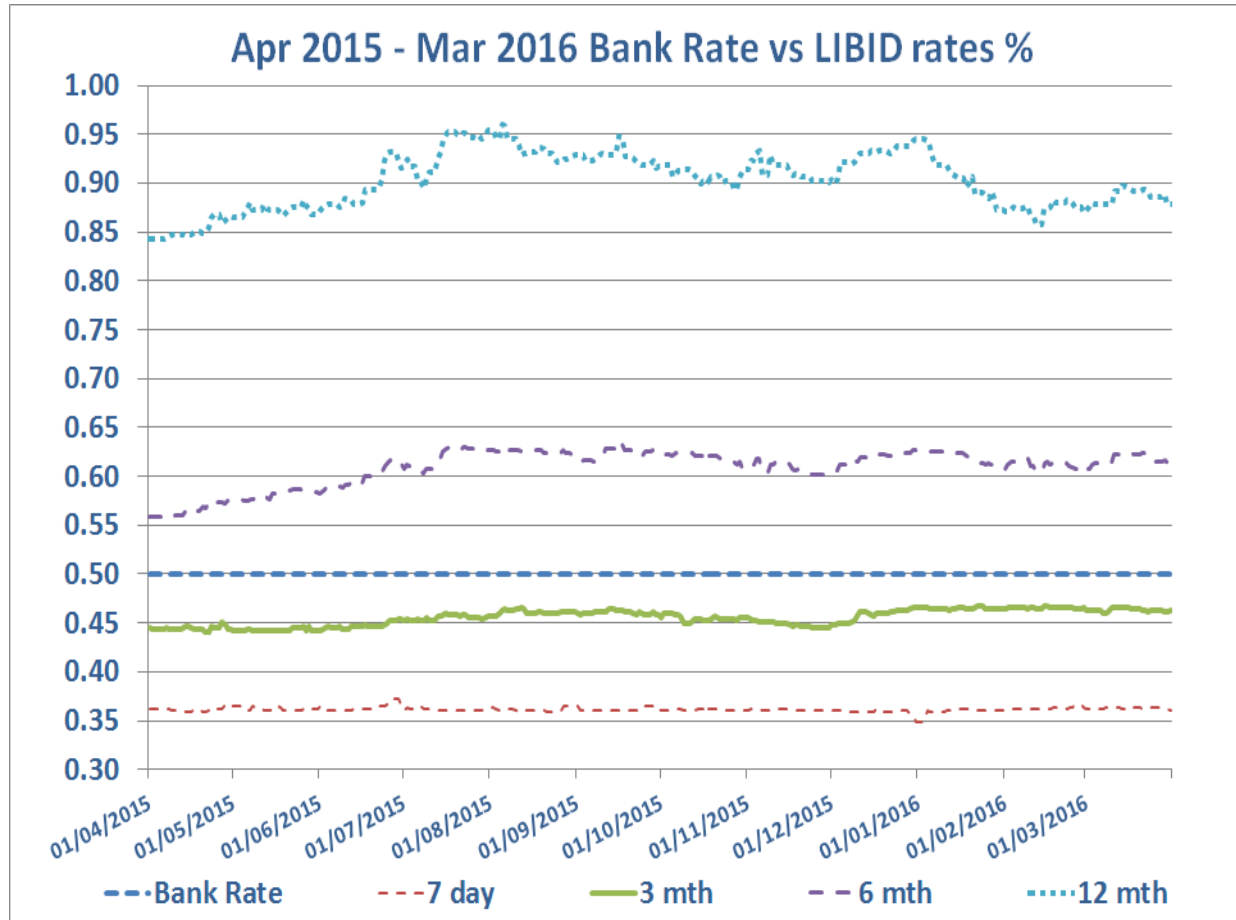
	1 Year	5 Year	10 Year	25 Year	50 Year
1/4/15	1.13%	1.90%	2.49%	3.15%	3.11%
31/3/16	1.13%	1.61%	2.28%	3.11%	2.92%
Low	1.01%	1.47%	2.10%	2.98%	2.81%
Date	11/02/2016	11/02/2016	11/02/2016	11/02/2016	11/02/2016
High	1.35%	2.35%	3.06%	3.66%	3.58%
Date	05/08/2015	14/07/2015	14/07/2015	02/07/2015	14/07/2015
Average	1.21%	2.00%	2.65%	3.35%	3.22%

Apr 2015 - Mar 2016 PWLB maturity certainty rates



## Investment Rates 2015-16

Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for seven years. Deposit rates remained depressed during the whole of the year, primarily due to the effects of the Funding for Lending Scheme.



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