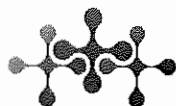


Nottinghamshire Police and Crime Commissioner
Notice of Decision



Nottinghamshire

POLICE & CRIME COMMISSIONER

Author:	Charlotte Radford
For Decision or Information	Decision and Information
Date received*:	19.11.15
Ref*:	2015.066

TITLE: Mid-Year Treasury Management Report 2015-16

EXECUTIVE SUMMARY:

The attached report is the mid-year position of treasury management performance compared with the approved strategy.

In addition to this a review has been undertaken internally by the Treasury Management Accountant on the calculation of the Minimum Revenue Provision. By making a slight change to how the MRP is calculated (i.e. move to average asset life) we are able to generate significant savings to the revenue budget in the current financial year and still comply with the policy for MRP. We would also generate significant savings in relation to the MRP charge for previous years and be able to reduce the amount held in the central MRP. It is recommended that the amount relating to previous years is transferred to reserves for use in closing the financial gap for the 2016-17 budget.

INFORMATION IN SUPPORT OF DECISION: (e.g. report or business case)

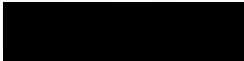
Report attached.

FINANCIAL INFORMATION (please include if is it capital or revenue or both. What the split is and the totals being requested. Is this a virement/ something already budgeted for or something that requires additional funding. Are there any savings that can be offered up/or achieved)

The capital programme for 2015-16 will be reduced from £20.177m to £16.172m with a potential further £3m slippage into the next financial year. Both of these positions are fundamentally different to the assumptions within the estimates that the approved strategy is based upon and a separate decision record exists for this change.

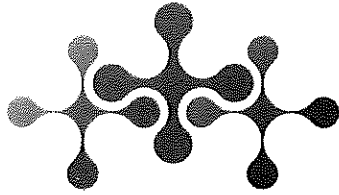
The resultant impact on the treasury management strategy is detailed within the attached report.

Further to this the review of MRP will result in £1.0m of savings against the current year revenue budget and an additional £0.9m reduction to the revenue account resulting from not delivering the full capital programme in 2014-15. This also means that £1.9m will be released from the Capital Adjustment Reserve into earmarked reserves for use towards financing part of next years budget gap.

Signature: 
 Chief Finance Officer

Date: 24th November 2015

Is any of the supporting information classified as non public or confidential information**?	Yes		No	✓
If yes, please state under which category number from the guidance**				



Nottinghamshire

POLICE & CRIME COMMISSIONER

**Treasury Management Strategy
Statement Mid-year Review Report
2015/2016**

**Incorporating Review of Minimum Revenue Provision
Policy and Annual Investment Strategy**

1 Background

The Nottinghamshire Office of the Police and Crime Commissioner (NOPCC) operates a balanced budget, which broadly means income raised during the year (plus planned spending from reserves) will meet its planned expenditure. The treasury management operation ensures the resulting cash flow is adequately planned, with surplus monies being invested in low risk counterparties. It provides adequate liquidity before considering optimising investment return.

The treasury management operation also arranges the funding of capital plans. These capital plans provide a guide to the borrowing need, and form the basis of longer term cash flow planning to ensure that the capital spending operations can be met. 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 risk or cost objectives.

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." The responsible officer for treasury management is Chief Finance Officer to the Police & Crime Commissioner (Chief Finance Officer).

2 Introduction

The Commissioner complies with the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management.

The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of treasury management activities.
- Creation and maintenance of Treasury Management Practices which set out the manner in which to achieve those policies and objectives.
- Reporting requirements

The Commissioner is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead.

Mid-year Review Report (this report) will update the Commissioner with the position regarding capital, and amend prudential indicators as necessary. It also monitors whether the treasury activity is meeting the strategy and whether any policies require revision. It includes an economic update for the first part of the financial year;

The Government's July Budget eased the pace of cut backs from achieving a budget surplus in 2018/2019 to 2019/2020. Monthly public sector deficit figures have indicated that the Chancellor's most recent target for 2015/2016 will not quite be met.

3.1.2 U.S.

GDP growth in 2014 of 2.4% was followed by first quarter 2015 growth depressed by exceptionally bad winter weather at only +0.6% (annualised). However, growth rebounded very strongly in Q2 to 3.7% (annualised) and strong growth is predicted. Until the turmoil in financial markets in August caused by fears about the slowdown in Chinese growth, it had been strongly expected that the Fed. would start to increase rates in September. However, while this did not happen it was a close decision, and is still expected later in 2015.

3.1.3 Eurozone

The ECB started a massive €1.1 trillion programme of quantitative easing between March 2015 and September 2016 to buy up high credit quality government debt of selected EZ countries. This seems to have already had a beneficial impact in improving market confidence. There has also been a continuing trend of marginal increases in the GDP growth rate which hit 0.4% in quarter 1 2015 (1.0% y/y) and +0.4% in Q2 GDP (1.5% y/y).

During July, Greece finally co-operated fully with EU demands to implement a major austerity programme. An €86bn third bailout package has recently been agreed. However, huge damage has been done to the Greek banking system and economy by the resistance of the Syriza Government, elected in January and re-elected in September.

3.1.3 China and Japan

Japan causes concern as an April 2014 increase in sales tax has suppressed consumer expenditure and growth. In Q2 2015 growth was -1.6% (annualised) after a short burst of strong growth of 4.5% in Q1. During 2015, Japan has been hit hard by the downturn in China. The outlook is not good because the Abe government is reluctant to reform inefficient areas of the economy due to political concerns. Recent stock market falls have caused the yen to strengthen against the dollar as it is considered a safe haven by investors in times of market tumult. This negatively impacts their large export market.

The Chinese Government has been very active during 2015 in implementing measures to try to ensure the economy hits the growth target of 7% for the current year. There are concerns that recent growth figures had been presented to mask a downturn. There are also major concerns as to the creditworthiness of bank lending during the post 2008 credit expansion period and whether housing prices would collapse. There is deepening concern regarding the health of the Chinese economy with shares in the region plummeting to their lowest level for three-and-a-half years in September, after weak Chinese data prompted sharp losses on

- The commencement by the US Federal Reserve of increases in the Fed. funds rate in 2015, causing a fundamental reassessment by investors of the relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.
- UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

4 The Commissioner's Office Capital Position (Prudential Indicators)

The Treasury Management Strategy Statement (TMSS) for 2015/2016 was approved by the Commissioner on 16 February 2015 (Decision record 2015/ 005). An update of that information is included here. There are no changes required to the limits set in this report.

4.1 Prudential Indicator for Capital Expenditure and Financing

This table shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the Budget. It also shows the anticipated method of financing.

The capital programme has been stringently reviewed to make savings and to ensure that capital plans are still fit for purpose in line with the 3 force strategic alliance. The borrowing element of the table increases the underlying indebtedness of the Commissioner's Office by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). This new borrowing need may also be supplemented by the need to replace maturing debt.

Capital Expenditure by Service

	2015-16 Original Estimate £m	Current Position £m	2015-16 Revised Estimate £m
Estates	7.266	1.610	6.165
IT	4.770	0.516	5.285
Other	8.141	1.596	4.722
Total	20.177	3.722	16.172
Financed by:			
Capital Receipts	1.369	1.369	1.369
Capital Grants	1.448	1.448	1.448
Total Financing	2.817	2.817	2.817
Borrowing need	17.360	0.905	13.355

4.2 Prudential Indicator Monitoring

	2014/2015 Authority Approved Indicator	2014/2015 Outturn @ 31/3/15	2015/2016 Authority Approved Indicator	2015/2016 Outturn @ 30/9/15
<u>Section 1 - Indicators Based on Expected Outcomes</u>				
<u>Affordability:</u>				
1) Ratio of Financing Costs to Net Revenue Stream	2.0%	2.0%	2.9%	2.0%
2) Incremental Impact of Capital Investment Decisions	£2.49	-	£7.08	-
3) Actual Capital Expenditure 30.09.15	-	-	-	£3.862m
Estimated Capital Expenditure 31.03.16	-	-	-	£15.668m
4) Capital Financing Requirement	£56.503m	£59.354m	£65.001m	£59.354m
<u>Section 2 - Indicators Based on Limits</u>				
<u>Affordability:</u>				
1) Actual External Debt 30.09.15	-	£30.816m	-	£31.853m
Estimated External Debt 31.03.16	-	-	-	£47.157m
2) Authorised Limit for External Debt	£70.000m	-	£75.000m	-
3) Operational Boundary for External Debt	£60.000m	-	£65.000m	-
<u>Prudence:</u>				
1) Net Borrowing Requirement & CFR	£56.503m	£61.871m	£65.306m	£66.007m

The Capital Financing Requirement is the underlying external need to incur borrowing for a capital purpose. This is calculated on using the best estimate of slippage of project managers at the date of writing (21 October). This is currently within the approved indicator. It also shows the expected debt position over the period, known as the Operational Boundary, the additional amount representing PFI and leasing liabilities.

A key control over treasury activity is a prudential indicator to ensure that over the medium term, net borrowing (borrowings less investments) will only be for capital purposes. Gross external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2015/2016 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Commissioner has approved a policy for borrowing in advance of need if this proves prudent. The Chief Financial Officer reports that no difficulties are envisaged for the current or future years in complying with this prudential indicator.

The Chief Financial Officer confirms that the approved limits within the Annual Investment Strategy were not breached during the first six months of 2015/2016.

The budgeted investment return for 2015/2016 is £0.210m and although the rate of return is higher than the performance benchmark for the year to date the forecast is £0.150m. This is because there have been lower levels of surplus to invest and the rates available for immediate access have continued to fall.

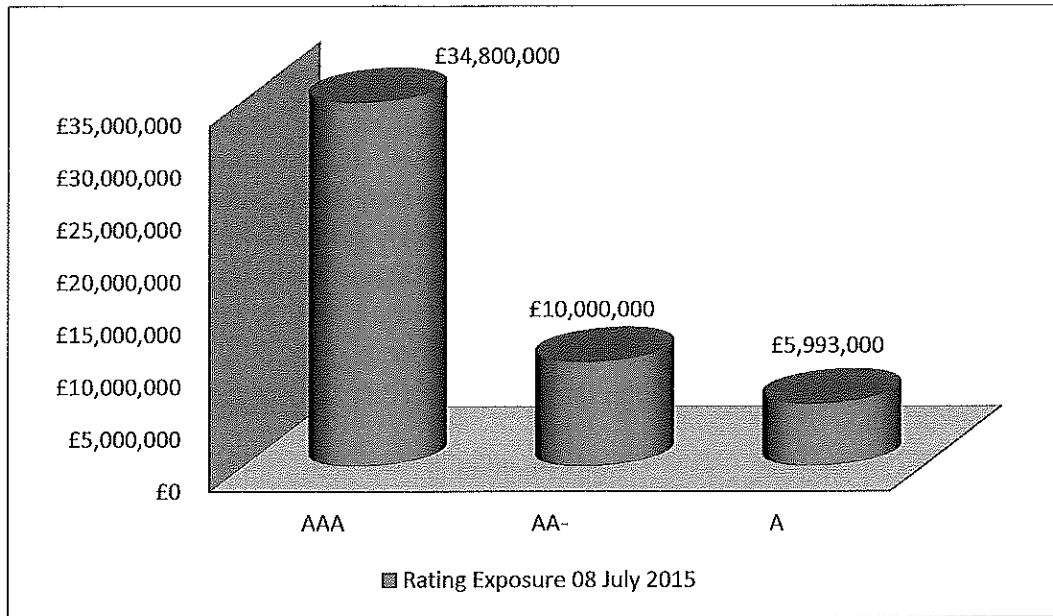
5.1 Investment Counterparty criteria

The Commissioner's investment policy has regard to the Department for Communities & Local Government's (CLG) and the revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sector Guidance Notes ("the CIPFA TM Code"). Therefore the Commissioner's investment priorities in order of importance will be security, liquidity and return.

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. Commencing in 2015, in response to the evolving regulatory regime, all three agencies have begun removing these "uplifts" with the timing of the process determined by regulatory progress at the national level. The process has been part of a wider reassessment of methodologies by each of the rating agencies. In addition to the removal of implied support, new methodologies are now taking into account additional factors, such as regulatory capital levels. In some cases, these factors have "netted" each other off, to leave underlying ratings either unchanged or little changed. A consequence of the new methodologies has also lowered the importance of the (Fitch) Support and Viability ratings and has seen the (Moody's) Financial Strength rating withdrawn by the agency.

In line with the revised methodologies, our own credit assessment process now focuses solely on the Short and Long Term ratings of an institution. While this is the same process that has always been used by Standard & Poor's, this has been a change to the use of Fitch and Moody's ratings. It is important to stress that the other key elements to our process, namely the assessment of Rating Watch and Outlook information as well as the Credit Default Swap (CDS) overlay have not been changed.

The evolving regulatory environment, in tandem with the rating agencies' new methodologies also means that sovereign ratings are now of lesser importance in the assessment process. Where through the crisis, clients typically assigned the highest sovereign rating to their criteria the new regulatory environment is attempting to break the link between sovereign support and domestic financial institutions. Although this factor now has less prominence NOPCC will continue to



5.2 Creditworthiness policy

The Chief Financial Officer will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to the Commissioner for approval as necessary. The minimum rating criteria uses the lowest common denominator method of selecting counterparties and applying limits. The current criteria incorporate the changes made by the ratings agencies in 5.1. No changes are recommended to the current counterparty criteria.

	Fitch Long term Rating (or equivalent)	Value Limit	Time Limit
Banks 1 higher quality	AAA	£5m	1 yr
Banks 1 medium quality	AA-	£5m	1 yr
Banks 1 medium / lower quality	A	£4m	6 months
Banks 1 lower quality	A-	£3m	100 days
Banks 2 — part nationalised	N/A	£5m	1yr
Limit 3 category — Commissioners banker (not meeting Banks 1)	AA	£5m	1 day
UK Govt - DMADF	AAA	Unlimited	6 months
Local authorities	N/A	£5m	2 yrs
Enhanced money market funds with instant access	AAA	£5-10m	liquid
Enhanced money market funds with notice	AAA	£3-5m	liquid

The general trend has been decreasing interest rates during the six months across longer dated maturity bands, but a rise in the shorter maturities, reflecting in part the expected rise in the Bank rate.

PWLB certainty rates, half year to 8th September 2015

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	1.11%	1.82%	2.40%	3.06%	3.01%
Date	02/04/2015	02/04/2015	02/04/2015	02/04/2015	02/04/2015
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	1.26%	2.14%	2.78%	3.40%	3.30%

7 Review of Minimum Revenue Provision Policy Statement Interpretation

7.1 Introduction

The Commissioner's Office repays each year part of the accumulated capital spend (CFR) through a revenue charge (MRP). An additional voluntary payment may also be made (VRP). The MRP can be calculated in various ways but the overarching principles are that the repayment must be prudent and affordable.

7.2 The Stated Policy

The existing policy was approved by The Commissioner on 16th February 2015. This policy has been used since 1st April 2008. It states that:

"For capital expenditure incurred before 1st April 2008 this is based on approximately 4% of the CFR (option 2)
For unsupported capital expenditure incurred after this date then the MRP is based on the asset life method (option 3)"

The way that this has been interpreted is that the 4% of the CFR has been calculated using a fixed amount based on values as at 1st of April 2008, as opposed to the value of the CFR at the date of calculation (reducing balance) which is now proposed to be the interpretation to be used.