Agenda Item No:	**9.1**	**Report No:**	**148/15**
Report Title:	**Finance Update**		
Report To:	**Cabinet**	**Date:**	**23 November 2015**
Cabinet Member:	**Councillor Bill Giles**		
Ward(s) Affected:	**All**		
Report By:	**Alan Osborne, Director of Corporate Services**		

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Purpose of Report:

To provide an update on financial matters affecting the General Fund Revenue Account, the Housing Revenue Account and the approved Capital Programme.

Officers Recommendation(s):

That Cabinet:

1 Agrees Treasury Management activity since the last report to Cabinet has been consistent with the Council's approved Treasury and Investment Strategy.

2 Agrees the mid-year position for the Council's 2015/2016 Treasury Management and Investment Strategy.

3 Agrees the General Fund and Housing Revenue Account financial performance for the quarter ended 30 September 2015 as set out in section 4.

4 Agrees the Capital Programme financial performance for the quarter ended 30 September 2015, and associated variations, as set out in section 5

5 Confirms the action taken in respect of procurement as set out in section 6.

Recommends to Council:

6 That Council approves the Mid-Year Treasury Management Report 2015/2016 at Appendix 1.

Reasons for Recommendations

1 A report on funding issues in relation to the Council's General Fund Revenue Account, Housing Revenue Account and Capital Programme is made to each meeting of the Cabinet to ensure that the Council's financial health is kept under continual review. It is essential to ensure that the Council has a sound financial base from which to respond to changing activity levels and demand for statutory services and to ensure that, when appropriate, its finances are adjusted in response to reducing income levels and inflationary pressures on expenditure.

2 The Council's Treasury Management function deals with very large value transactions on a daily basis. It is essential that the Council is satisfied that appropriate controls are in place and in accordance with the Code of Practice on Treasury Management in the Public Services prepared by CIPFA (the Chartered Institute of Public Finance and Accountancy) and adopted by the Council.

Information

3 Treasury Management

3.1 Treasury Management investment activity between 22 August and 19 October 2015 is summarised in the table below. All activity was consistent with the Council's approved Treasury and Investment Strategy for 2015/2016.

Type of investment	New investments	Matured investments	Average on deposit £m	Average return %
Short term deposits	£30.5m	£23.5m	8.90	0.35
Long term deposits	Nil	Nil	0.00	0.00
Treasury Bills	£5.0m	£6.0m	9.61	0.48
Money Market Funds	daily		5.52	0.55
Interest Bearing Accounts			2.54	0.40

3.2 No new borrowing was undertaken in the period. Long term borrowing remains at £56.6m.

3.3 In accordance with the Council's approved Treasury Strategy Statement, the Audit and Standards Committee reviews all treasury activity that takes place in order to confirm that it has been undertaken in accordance with the approved Strategy. Should the Audit and Standards Committee have any observations they would be recorded in its minutes and referred to Cabinet.

Mid Term Treasury Management and Investment Strategy Review

3.4 CIPFA's Code of Practice recommends that all councillors are informed of Treasury Management activities at least twice a year. A Mid-year Report for 2015/2016, which covers the period 1 April 2015 to 30 September 2015, is attached at Appendix 1. The Report confirms that the key elements of the approved Treasury and Investment Strategy have been complied with during the first half of the year.

3.5 Cabinet is asked to recommend that Council approves the Mid-year Report at its meeting on 9 December 2015. The Audit and Standards Committee will be presented with the Report on 30 December 2015 - any comments that it may wish to pass on to Council will be reported verbally

4 Financial Performance – Revenue budgets

4.1 Financial Performance at the end of Quarter 2 (September) 2015/2016 is shown below. Service details are shown at Appendix 2.

Activity	Full year budget £'000	Qtr 2 Profiled Budget £'000	Qtr 2 actual £'000	Qtr 2 variance £'000
Service Delivery				
Housing and Environment	1,638	1,519	1,293	(226)
Planning and Revenues	1,716	(4,133)	(4,409)	(276)
Customer Service	1,482	962	898	(64)
Waste and Recycling	2,771	1,445	1,422	(23)
	7,607	(207)	(796)	(589)
Business Strategy and Development				
Business Strategy and Performance	662	310	326	16
Regeneration and Investment	1,021	391	231	(160)
Strategic Policy	545	245	189	(56)
	2,228	946	746	(200)
Corporate Services				
Property and Facilities	2,469	509	441	(68)
Legal	499	225	267	42
Democratic Services	899	427	344	(83)
Human Resources	538	238	214	(24)
Information Technology	1,565	720	812	92
Finance	990	391	344	(47)
Audit, Fraud and Procurement	310	134	136	2
	7,270	2,644	2,558	(86)
Corporate Strategy and Programmes	1,158	419	550	131
Financing, interest, grants, etc	(12,588)	(1,850)	(1,682)	168
Central Support Service recharges	(5,675)	(59)	(76)	(17)
Housing Revenue Account	0	(4,558)	(4,767)	(209)
TOTAL	**0**	**(2,665)**	**(3,467)**	**(802)**

4.2 Financial performance in the first quarter resulted in a favourable net variation of £802,000. This builds on the Quarter 1 position reported to Cabinet in September. Key elements of this variation were:

	£'000
Employee costs – the savings delivery plan assumes a vacancy savings target of 2% for the year. At the end of Quarter 2, in year savings from vacant posts exceeded the target by 4%	(220)
Staff severance costs – costs incurred as part of corporate restructuring	86
Planning Development Control fees –income in Quarter has continued to exceed the profiled budget	(119)
Business Rates local discount scheme - £370,000 has been earmarked to support a pilot scheme. At the end of Quarter 2 only 2 (minor) discounts have been awarded on application.	(180)
Government grants received – funding has been received in respect of the Neighbourhood Planning process and electoral registration changes and, in Quarter 2, costs associated with changes in the requirements for land charges fee setting	(106)
Recyclate sales – the budget for this income stream is £350,000. As reported at the end of Quarter 1 the market for recyclates is restricted. An overall shortfall against the budget for the year of £250,000 continues to be anticipated.	170
Green Waste collection service – this trial service in Seaford has been operational since August	(24)
Housing Revenue Account repairs	(57)
Planned repairs at General Fund property eg offices, parks, etc	(83)
	(533)

4.3 Spending activity in many service areas has continued to be slow in Quarter 2 and the 'gap' between budgeted and actual spend is expected to close in Quarter 3. Trends in housing benefit awarded and associated government subsidy due will also be more identifiable when the position is next reported.

5 Financial Performance – Capital Programme

5.1 Appendix 3 gives details of the capital programme spending in Quarter 2, which continues to be in line with expectations at this stage of the year. Payments of £1m were made in the quarter.

5.2 Cabinet is recommended to approve one variation in the programme, in respect of the Electric Vehicle Charging Points project. This initiative, led by Lewes District Council on behalf of the Sussex Air Quality Partnership is wholly funded by Government grant. 18 rapid chargers have now been installed across South East England, including 2 within the Lewes District area. This project is fully funded by Government grant and a third party contribution. The Government funding period closed on 30 September 2015. No further chargers will be installed after that date.

6 Procurement

6.1 The Council is implementing the Community Infrastructure Levy (CIL) from 1 December 2015. As previously reported to Cabinet, The administration of CIL is a complex process involving the processing, acknowledging and recording of a series of events or triggers and CIL documents. The Council is under a statutory duty to record and monitor its spending of CIL and produce annual reports thereon.

6.2 The need to procure a new or upgraded software system for the management and administration of Section 106 agreements and the CIL is considered fundamental to the proper implementation of the Council's CIL Charging Schedule. It should ensure the accurate and expedient delivery of CIL processes and ultimately aid the delivery of infrastructure projects. It is important that the CIL software fulfils a range of activities required by the CIL Regulations and interacts with the existing planning (Uniform), land charges (TLC) and finance (Agresso) systems. It is also important that the software choice is aligned with the software package to be implemented by Eastbourne Borough Council (EBC) in order to ensure effective use of resources in a shared service environment.

6.3 Officers have analysed available software solutions and sought quotations from three suppliers. Of these, two do not adequately meet the Council's requirements, with the preferred supplier being the most expensive. The Council's Contract Procedure Rules require the Head of Service to approve the acceptance of a quotation which is other than the lowest, and this action has now been taken. The cost of implementing the software system, £25,000, will be met from the budget for Service Priorities. Future costs will be funded from a 5% share of CIL receipts retained as an administration 'pot'.

7 Financial Appraisal - referred to under individual items above.

8 Legal Implications - there are no legal implications arising from this report.

Risk Management Implications

8.1 The Council maintains an overview of its policy programme, its Medium Term Financial Strategy and the external factors that affect them. Without this constant analysis and review there is a risk that the underlying recurring revenue budgets will grow at a faster rate than the resources available to fund them. This risk is mitigated through regular reports to Cabinet on the Council's overall revenue and capital position and Cabinet's correcting actions taken in accordance with the objectives and principles it set for management of the Council's finances.

8.2 An additional risk in the current climate is that reserves and balances will be drawn upon sooner than is necessary unless an assessment is made of resource implications where activity levels have fallen or risen to any significant degree. This risk is mitigated by identifying such areas, making an assessment covering the short and medium term and taking corrective action.

9 Equality Screening

This Finance Update is a routine report for which detailed Equality Analysis is not required to be undertaken. The equality implications of individual decisions relating to the projects/services covered in this report are addressed within other relevant Council reports.

Background Papers:

Treasury Strategy Statement http://www.lewes.gov.uk/council/20987.asp

Appendices

Appendix 1 – Mid-year Treasury Management Report 2015/2016
Appendix 2 – Financial performance Quarter 2 by service
Appendix 3 – Capital Programme 2015/2016 – Quarter 2

APPENDIX 1

Lewes District Council

Mid-year Treasury Management Report 2015/2016

Contents

1. Background

1.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management (the Code) recommends that full Council should receive every year reports on Treasury Management policies and activity before the start of the year, mid-year and after the end of the year. The intention is that those with ultimate responsibility for the Treasury Management function appreciate fully the implications of Treasury Management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

1.2 The Council defines its Treasury Management activities as:

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

1.3 This mid-year report covers the period 1 April to 30 September 2015.

2. Overall Summary of Activity

2.1 At its meeting in February 2015, the Council agreed its Treasury Management Strategy Statement and Investment Strategy 2015/16 to 2017/18. The table below lists the key elements of that Strategy and records actual performance in the first six months of the year against each one of them.

Key Element	Target in Strategy	Actual Performance	
Borrowing			
Underlying need to borrow (CFR) at year end	£74.034 million	£77.534 million (projection 31 March)	-
Internal borrowing at year end	£17.361 million	£20.861 million (projection 31 March)	-
New external long-term borrowing in year	None anticipated	None undertaken Apr to Sept '15.	✓
Debt rescheduling in year	Review options but not anticipated	Options kept under review, none undertaken Apr to Sept' 15. Potential identified for March 2015	✓
Interest payments on external borrowing	£1.730 million	£0.864m (to date)	✓
Investments			
Minimum counterparty credit ratings for investments of up to 1 year	Long-term A (does not apply to Government and other local authorities which have the highest ratings)	At least Long-term A	✓
Interest receipts from external investments	£0.075m	£0.074m (to date)	✓

Key Element	Target in Strategy	Actual Performance	
Appointment of Investment Consultants			
Independent Treasury Adviser to be retained	Arlingclose to be retained as Treasury Adviser	Arlingclose retained as Treasury Adviser	✓
Reporting and Training			
Reports to be made to Audit and Standards Committee and Cabinet	Every meeting	Every meeting	✓
Briefing sessions for Councillors and Staff	Treasury Adviser to provide	Arlingclose scheduled to meet with Councillors and Staff October 2015	✓

2.2 For those who are looking for more than this overall confirmation that all treasury management and investment activity in 2015/2016 has been carried out in accordance with the Council's agreed Strategy, the remainder of this report analyses each of the key elements in more depth. Appendix A, supplied by Arlingclose explores the economic background to the year's activity and Appendix B lists all term deposits made in the first half of the year. A Glossary appears at the end of the document to explain the technical terms which could not be avoided when writing this report.

3. Detailed Analysis - Borrowing

3.1 Other than for temporary cash flow purposes, local authorities are only allowed to borrow to finance capital expenditure (eg the purchase of property, vehicles or equipment which will last for more than one year, or the improvement of such assets). The Government limits the amount borrowed by local authorities for housing purposes only by specifying 'debt caps'. This Council's underlying debt cap has been fixed at £72.931m. In 2014/2015 local authorities were able to bid for an increase in the housing debt cap in order to enable specific development projects to take place. A bid from this Council was successful and the debt cap has been increased to £75.248m to incorporate spending on 7 new build projects which will deliver 30 new homes in total.

3.2 In accounting terms, the underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). This, together with Balances and Reserves, are the core drivers of Treasury Management activity.

3.3 The CFR is, in simple terms, the amount of capital expenditure which has been incurred by the Council but which has not yet been paid for (by using, for example, grants, capital receipts, reserves or revenue income) and in the meantime is covered by internal or external borrowing. External borrowing is where loans are raised from the Public Works Loans Board or banks. Alternatively it is possible to use the cash which has been set aside in Balances and Reserves and which would otherwise need to be invested with banks or other borrowers as a means to avoid taking on external loans. This is known as internal borrowing.

3.4 As noted above, the level of CFR increases each year by the amount of unfinanced capital expenditure and is reduced by the amount that the Council sets aside for the repayment of borrowing. The original CFR projection for 2015/2016, along with an updated analysis, is shown in the table below. The increases in capital expenditure and financing shown reflect the approved capital programme as at September 2015, and assume that all projects are completed in the year. That outcome is unlikely however - the capital programme represents an allocation of funds to specific long-term projects many of which span financial years, for example the construction of a new depot facility at a projected cost of £3.5 million.

3.5 As at 30 September 2015, capital expenditure with a total value of £3.8m had been incurred (excluding commitments) compared with the approved capital programme of £25.6m (including £6.7m brought forward from 2014/2015). All capital expenditure will be funded from existing capital resources, with the exception of the construction of the new Depot facility in Avis Way, Newhaven, the shared community hub in Newhaven, the photovoltaic panel installation programme and the construction of new affordable homes.

	2015/16 Original £m	2015/16 Projected £m
Opening CFR	70.709	69.799
Capital expenditure in year (projected)	15.666	25.591
Less financed	(10.464)	(16.203)
Less amount set aside for debt repayment	(1.877)	(1.833)
Closing CFR	74.034	77.534

3.6 The overall CFR can be split between the General Fund and Housing Revenue Account as follows:

	2015/16 Original £m	2015/16 Projected £m
General Fund CFR	8.421	11.237
Housing Revenue Account CFR	65.613	66.297
Total CFR	74.034	77.534

3.7 The following table compares the CFR with the amount that the Council holds in balances and reserves as well as working capital (day to day cash movements as well as grants, developer contributions and capital receipts held pending use):

	31/3/16 Original £m	31/3/16 Projected £m
(a) Capital Financing Requirement	74.034	77.534
(b) Actual external borrowing	(56.673)	(56.673)
(c) Use of Balances and Reserves and working capital as alternative to borrowing (a)–(b)	17.361	20.861

3.8 Total interest paid on long-term borrowing in the period to 30 September 2015 was £0.864 million, representing the first of two instalments of interest due on the Council's loans from the PWLB and a £5 million market Lender's Options Borrower's Option (LOBO) loan at the rate of 4.5% with a term of 50 years. Under the terms of the LOBO, the Lender will next review the rate/terms of the loan in April 2016 and if it proposes an increase, the Council will have an option to repay.

3.9 The Council qualifies for new borrowing at the ‘Certainty Rate’ (0.20% below the PWLB standard rate) in 2015/2016. In the period to September 2015, no new borrowing, either long-term or short-term (for cash flow purposes) had been undertaken.

3.10 Through the year, officers, supported by Arlingclose, monitor opportunities for the rescheduling of external loans and the possibility of repayment utilising cash balances that would otherwise be invested. The borrowing portfolio (£56.673m in total) includes one £5m PWLB variable rate loan with a maturity date in March 2022. The rate of interest on this loan is reviewed by the Government every six months (in September and March).

3.11 A review of the Council’s position in September 2015, suggests that it might be cost effective to repay the £5m PWLB variable rate loan in March 2016. This external borrowing would be replaced by utilising reserves and balances and working capital, reducing the amount held for investment and its associated risk. An alternative would be to enter into long-term investments with a total value in excess of £5m, locking in a return in excess of the variable borrowing rate. At 31 March 2016, a minimum of £20.9m is expected to be held, comprising reserves and balances, £11.7m, and working capital, £9.2m. In early 2016, Arlingclose, the Council’s Treasury Advisors will support the Council in determining the most appropriate approach in the light of market conditions at that time.

4. Detailed Analysis - Investments

4.1 The Council held on average £22.84 million available for investment in the period to 30 September 2015. This comprised working cash balances, capital receipts, earmarked reserves and developer contributions held pending use.

4.2 The Council’s general policy objective is to invest its surplus funds prudently. The Council’s investment priorities have continued to be:

highest priority - security of the invested capital;
followed by - liquidity of the invested capital;
finally - an optimum yield commensurate with security and liquidity.

4.3 All of the Council’s investments have been managed in-house. Security of capital has been maintained by following the counterparty policy set out in the Investment Strategy for 2015/2016. Investments during the period included:

- Fixed Term Deposits with the Debt Management Office (total £76.25 million)
- Fixed Term Deposits with other Local Authorities (total £7.00 million)
- Fixed Term Deposits with UK Banks/Building Societies (total £6.00 million)
- Investments in AAA-rated Constant Net Asset Value Money Market Funds (MMFs) (average balance held in year £5.51 million)
- United Kingdom Treasury Bills (average balance £8.30 million)
- Deposit accounts with UK Banks (average balance held in year £1.59 million)
- Overnight deposits with the Council’s banker, Lloyds Bank (average balance held in year £0.94 million)

4.4 The Council has approved the use of two MMFs, DB Advisors – Deutsche Global Liquidity Series and Goldman Sachs Asset Management International.

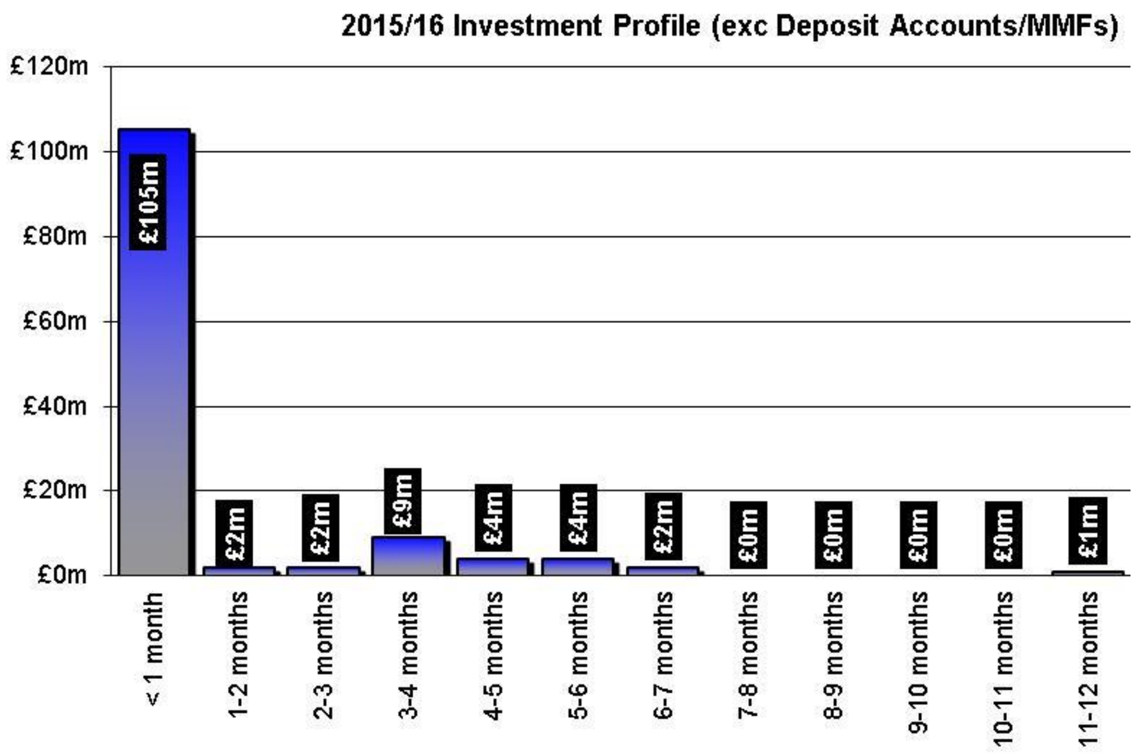
4.5 Counterparty credit quality was assessed and monitored with reference to credit ratings (a minimum long-term counterparty rating of A across all three rating agencies Fitch, Standard and Poors, and Moody's applied); credit default swaps; GDP of the country in which the institution operates; the country's net debt as a percentage of GDP; any potential support mechanisms and share price.

4.6 In keeping with Government guidance on investments, the Council maintained a sufficient level of liquidity through the use of MMFs, overnight deposits and deposit accounts.

4.7 In September 2015, Cabinet agreed that a nominee account should be opened with a second broker to allow a maximum of £20m to be invested in negotiable instruments (eg Treasury Bills) at any one time. The Investment Strategy limits the amount that can be held in a single broker's account to £10m and Cabinet's decision increases the opportunity to make these investments in the second half of 2015/2016.

4.8 The Council sought to optimise returns commensurate with its objectives of security and liquidity. As expected when setting the investment income budget for 2015/2016, the UK Bank Rate has been maintained at 0.5%.

4.9 A full list of temporary deposits made in the year is given at Appendix B. All investments were made with UK institutions, and no new deposits were made for periods in excess of one year. The chart below gives an analysis of fixed term deposits by duration.



4.10 Interest generated from investments in the year to date was £0.074 million, just below the total 2015/2016 budget for investment income £0.075 million. The projected return to the year end indicates that the budget may be exceeded by £0.030 million. This favourable position has arisen as a result of higher than anticipated levels of cash being held pending expenditure on capital programme projects, etc.

4.11 The average rate of return from investments at the end of Quarter 1 and Quarter 2 is shown in the table below, along with comparative benchmark information from the Arlingclose client base. The return is below the benchmark, reflecting the very low credit risk and low duration of the Council's investment portfolio.

	Lewes District Council	Arlingclose client base
Average rate of investments 30 June 2015	0.46%	0.64%
Average rate of investments 30 September 2015	0.49%	0.66%

5. Counterparty Update

5.1 All three credit ratings agencies have reviewed their ratings in the six months to reflect the loss of government support for most financial institutions and the potential for varying loss given defaults as a result of new bail-in regimes in many countries. Despite reductions in government support many institutions have seen upgrades due to an improvement in their underlying strength and an assessment that that the level of loss given default is low.

5.2 Fitch reviewed the credit ratings of multiple institutions in May. Most UK banks had their support rating revised from 1 (denoting an extremely high probability of support) to 5 (denoting external support cannot be relied upon). This resulted in the downgrade of the long-term ratings of Royal Bank of Scotland (RBS) to BBB+ from A, Deutsche Bank to A from A+, Bank Nederlandse Gemeeten to AA+ from AAA and ING to A from A+. JP Morgan Chase and the Lloyds Banking Group however both received one notch upgrades.

5.3 Moody's concluded its review in June and upgraded the long-term ratings of Close Brothers, Standard Chartered Bank, ING Bank, Goldman Sachs International, HSBC, RBS, Coventry Building Society, Leeds Building Society, Nationwide Building Society, Svenska Handelsbanken and Landesbank Hessen-Thueringen.

5.4 S&P reviewed UK and German banks in June downgrading Barclays' long-term rating to A- from A, RBS to BBB+ from A- and Deutsche Bank to BBB+ from A. S&P has also revised the outlook of the UK as a whole to negative from stable, citing concerns around a planned referendum on EU membership and its effect on the economy.

5.5 At the end of July, the council's treasury advisors Arlingclose advised an extension of recommended durations for unsecured investments in certain UK and European institutions following improvements in the global economic situation and the receding threat of another Eurozone crisis. A similar extension was advised for some non-European banks in September, with the Danish Danske Bank being added as a new recommended counterparty and certain non-rated UK building societies also being extended.

5.6 At 30 September 2015, the following UK institutions met the Council's investment criteria and were potential counterparties:

Bank of Scotland plc	Barclays Bank plc
Close Brothers Ltd	Goldman Sachs International Bank
HSBC Bank plc	Lloyds Bank plc
Santander UK plc	Standard Chartered Bank
Coventry Building Society	Nationwide Building Society

A number of non-UK institutions also met the criteria, although there is very limited opportunity to place deposits with these institutions.

6. Banking Arrangements

Lloyds Bank plc was appointed as the Council's banker in 2014/2015 and accounts have been in operation since 1 September 2014.

7. Internal Borrowing

7.1 Following the national reform of housing finance, since 1 April 2012 the Council has adopted a 'two pool' approach to the accounting treatment of loans. Under this approach, interest on any external borrowing in respect of expenditure on General Fund services is to be charged to the General Fund, and interest on any external borrowing in respect of the Council's housing stock (Housing Revenue Account (HRA)) is to be charged to the HRA. At the start of the year, all external borrowing was attributed to the HRA.

7.2 Where the HRA or General Fund has surplus cash balances which allow either account to have external borrowing below its level of CFR (internal borrowing), the approved Treasury Strategy explains that the rate charged on this internal borrowing will be based on the rate of interest applicable to a one-year maturity loan from the PWLB at the start of the financial year.

7.3 It is expected that an interest payment will be made from the HRA to the General Fund in 2015/2016, but the final amount will not be determined until the close of the year, dependent on the capital programme outturn for the year. The HRA capital programme at 30 September 2015 includes £4.10m in respect of the construction or acquisition of new properties, to be part-funded by borrowing but it is not expected to take new loans from the PWLB or other source. This constitutes internal borrowing by the HRA from the General Fund and an interest charge will be made as outlined above.

8. Compliance with Prudential Indicators

The Council can confirm that it has complied with its Prudential Indicators for 2015/2016, which were set in February 2015 as part of the Council's Treasury Management Strategy Statement. Actual borrowing has remained within the Authorised Limit for External Debt (£72.5m) and the Operational Boundary for

External Debt (£67.0m).

9. Reporting and Training

9.1 The Director of Finance has reported the details of treasury management activity to each meeting of the Audit and Standards Committee and Cabinet held to date in 2015/2016.

9.2 All councillors tasked with treasury management responsibilities, including scrutiny of the treasury management function, were offered the opportunity to attend a local briefing session led by Arlingclose on 12 October 2015.

9.3 The training needs of the Council's treasury management staff continue to be reviewed as part of the annual corporate staff appraisal/training needs assessment process for all Council employees. Staff continue to attend Arlingclose workshops, when appropriate to their needs, alongside colleagues from other local authorities during 2015/2016.

10. Investment Consultants

Arlingclose have been retained as the Council's treasury advisor through the period covered by this report, under the terms of a four year contract which runs to 31 August 2016.

Appendix A – Economic Background explained by Arlingclose

As the year began, economic data was largely overshadowed by events in Greece. Markets' attention centered on the never-ending Greek issue stumbled from turmoil to crisis, running the serious risk of a disorderly exit from the Euro. The country's politicians and the representatives of the 'Troika' of its creditors - the European Commission (EC), the European Central Bank (ECB) and the International Monetary Fund (IMF) – barely saw eye to eye. Greece failed to make a scheduled repayment to the IMF on 30th June, in itself not a default until the IMF's Managing Director declares it so. Prime Minister Tsipras blindsided Greece's creditors by calling a referendum on 5th July on reform proposals which by then were off the table anyway. The European Central Bank froze liquidity assistance provided to Greek banks and capital controls within the country severely restricted individuals' and corporates' access to cash.

On 12th July, following a weekend European Union Summit, it was announced that the terms for a third bailout of Greece had been reached. The deal amounting to €86 billion was agreed under the terms that Greece would see tax increases, pension reforms and privatisations; the very reforms Tsipras had vowed to resist. This U-turn saw a revolt within the ruling Syriza party and on 27th August, Alexis Tsipras resigned from his post as Prime Minster of Greece after just eight months in office by calling a snap election, held on 20th September. This gamble paid off as Tsipras led his party to victory once again, although a coalition with the Independent Greeks was needed for a slim parliamentary majority. That government must now continue with the unenviable task of guiding Greece through the continuing economic crisis – the Greek saga is far from over.

The summer also saw attention shift towards China as the Shanghai composite index (representing China's main stock market), which had risen a staggering 50%+ since the beginning of 2015, dropped by 43% in less than three months with a reported $3.2 trillion loss to investors, on the back of concerns over growth and after regulators clamped down on margin lending activity in an effort to stop investors borrowing to invest and feeding the stock market bubble. Chinese authorities intensified their intervention in the markets by halting trading in many stocks in an attempt to maintain market confidence. They surprised global markets in August as the People's Bank of China changed the way the yuan is fixed each day against the US dollar and allowed an aggressive devaluation of the currency. This sent jitters through Asian, European and US markets impacting currencies, equities, commodities, oil and metals. On 24th August, Chinese stocks suffered their steepest one-day fall on record, driving down other equity markets around the world and soon becoming known as another 'Black Monday'. Chinese stocks have recovered marginally since and are trading around the same level as the start of the year. Concerns remain about slowing growth and potential deflationary effects.

UK Economy: The economy has remained resilient over the last six months. Although economic growth slowed in Q1 2015 to 0.4%, year/year growth to March 2015 was a relatively healthy 2.7%. Q2 2015 GDP growth bounced back and was confirmed at 0.7%, with year/year growth showing slight signs of slowing, decreasing to 2.4%. GDP has now increased for ten consecutive quarters, breaking a pattern of slow and erratic growth from 2009. The annual rate for consumer price inflation (CPI) briefly turned negative in April, falling to -0.1%, before fluctuating between 0.0% and 0.1% over the next few months. In the August Quarterly Inflation Report, the Bank of England projected that GDP growth will continue around its average rate since 2013. The Bank of England's projections for inflation remained largely unchanged from the May report with them expecting inflation to gradually increase to around 2% over the next 18 months and then remain there in the near future. Further improvement in the labour market saw the ILO unemployment rate for the three months to July fall to 5.5%. In the September report, average earnings excluding bonuses for the three months to July rose 2.9% year/year.

The outcome of the UK general election, largely fought over the parties' approach to dealing with the consequences of the structural deficit and the pace of its removal, saw some very big shifts in the political landscape and put the key issue of the UK's relationship with the EU at the heart of future politics.

Market reaction: Equity markets initially reacted positively to the pickup in the expectations of global economic conditions, but were tempered by the breakdown of creditor negotiations in Greece. China led stock market turmoil around the globe in August, with the FTSE 100 falling by around 8% overnight on 'Black Monday'. Indices have not recovered to their previous levels but some improvement has been seen. Government bond markets were quite volatile with yields rising (i.e. prices falling) initially as the risks of deflation seemingly abated. Thereafter yields fell on the outcome of the UK general election and assisted by reappraisal of deflationary factors, before rising again. Concerns around China saw bond yields dropping again through August and September. Bond markets were also distorted by the size of the European Central Bank's QE programme, so large that it created illiquidity in the very markets in which it needed to acquire these bonds, notably German government bonds (bunds) where yields were in negative territory.

Outlook for Q3 and Q4 2015/16

Arlingclose's expectation for the first rise in the Bank Rate (base rate) remains the second calendar quarter of 2016. The pace of interest rate rises will be gradual and the extent of rises limited. The appropriate level for Bank Rate for the post-crisis UK economy is likely to be lower than the previous norm. We would suggest this is between 2.0% and 3.0%. There is also sufficient momentum in the US economy for the Federal Reserve to raise interest rates in 2015, although risks of issues from China could possibly push this back.

The weak global environment and resulting low inflation expectations are likely to dampen long term interest rates. We project gilt yields will follow a shallow upward path in the medium term, with continuing concerns about the Eurozone, and other geo-political events, weighing on risk appetite, while inflation expectations remain subdued. The uncertainties surrounding the timing of UK and US interest rate rises, and the Chinese stock market-led turmoil, are likely to prompt short term volatility in gilt yields.

	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Average
Official Bank Rate														
Upside risk			0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.32
Arlingclose Central Case	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.75	1.75	1.08
Downside risk				-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-1.00	-1.00	-1.00	-1.00	-0.70

Appendix B – Term deposits made and/or maturing April to September 2015

Loan	Counterparty	Principal	From	To	Rate
220714	Barclays Bank plc	1,000,000	13 Aug 14	13 Aug 15	1.0000%
222514	Telford and Wrekin Council	3,000,000	6 Feb 15	15 Apr 15	0.4000%
222815	Debt Management Office	2,000,000	1 Apr 15	7 Apr 15	0.2500%
222915	Nationwide Building Society	1,000,000	8 Apr 15	8 Jul 15	0.5000%
223015	Debt Management Office	1,000,000	15 Apr 15	20 Apr 15	0.2500%
223115	Debt Management Office	2,000,000	6 May 15	21 May 15	0.2500%
223215	Nationwide Building Society	1,000,000	6 May 15	6 Aug 15	0.5000%
223315	Debt Management Office	2,500,000	7 May 15	8 May 15	0.2500%
223415	Debt Management Office	1,000,000	8 May 15	11 May 15	0.2500%
223515	Debt Management Office	1,000,000	8 May 15	18 May 15	0.2500%
223615	Debt Management Office	1,500,000	15 May 15	19 May 15	0.2500%
223715	Debt Management Office	1,500,000	15 May 15	21 May 15	0.2500%
223815	Debt Management Office	2,500,000	1 Jun 15	8 Jun 15	0.2500%
223915	Debt Management Office	1,000,000	3 Jun 15	9 Jun 15	0.2500%
224015	Debt Management Office	3,000,000	8 Jun 15	22 Jun 15	0.2500%
224115	Debt Management Office	3,000,000	15 Jun 15	22 Jun 15	0.2500%
224215	Debt Management Office	1,000,000	22 Jun 15	25 Jun 15	0.2500%
224315	Debt Management Office	1,750,000	25 Jun 15	2 Jul 15	0.2500%
224415	Plymouth City Council	2,000,000	30 Jun 15	1 Jul 15	0.3500%
224515	Debt Management Office	3,000,000	2 Jul 15	13 Jul 15	0.2500%
224615	Nationwide Building Society	1,000,000	8 Jul 15	8 Oct 15	0.5000%
224715	Debt Management Office	2,000,000	13 Jul 15	20 Jul 15	0.2500%
224815	Debt Management Office	4,000,000	15 Jul 15	21 Jul 15	0.2500%
224915	Debt Management Office	3,000,000	21 Jul 15	27 Jul 15	0.2500%
225015	Debt Management Office	3,000,000	27 Jul 15	7 Aug 15	0.2500%
225115	Coventry Building Society	2,000,000	3 Aug 15	3 Dec 15	0.5000%
225215	Debt Management Office	2,000,000	3 Aug 15	7 Aug 15	0.2500%
225315	Debt Management Office	6,000,000	3 Aug 15	10 Aug 15	0.2500%
225415	Debt Management Office	1,000,000	6 Aug 15	10 Aug 15	0.2500%
225515	Debt Management Office	4,000,000	10 Aug 15	14 Aug 15	0.2500%
225615	Nationwide Building Society	1,000,000	10 Aug 15	10 Feb 16	0.6600%
225715	Debt Management Office	4,000,000	14 Aug 15	17 Aug 15	0.2500%
225815	Debt Management Office	2,000,000	17 Aug 15	19 Aug 15	0.2500%
225915	Debt Management Office	3,000,000	17 Aug 15	24 Aug 15	0.2500%
226015	Debt Management Office	2,500,000	24 Aug 15	28 Aug 15	0.2500%
226115	Debt Management Office	1,500,000	28 Aug 15	7 Sep 15	0.2500%
226215	Debt Management Office	5,000,000	1 Sep 15	11 Sep 15	0.2500%
226315	Thurrock Borough Council	2,000,000	23 Sep 15	11 Feb 16	0.4700%
226415	Debt Management Office	1,000,000	3 Sep 15	11 Sep 15	0.2500%
226515	Debt Management Office	2,000,000	14 Sep 15	23 Sep 15	0.2500%
226615	Debt Management Office	2,500,000	15 Sep 15	21 Sep 15	0.2500%
226715	Newport City Council	3,000,000	23 Sep 15	7 Oct 15	0.4000%

Glossary of Terms

Affordable Borrowing Limit	Each local authority is required by statute to determine and keep under review how much money it can afford to borrow. The Prudential Code (see below) sets out how affordability is to be measured.
Base Rate	The main interest rate in the economy, set by the Bank Of England, upon which other rates are based.
Basis Point	A convenient way of measuring an interest rate (or its movement). It represents 1/100th of a percentage point, ie 100 basis points make up 1%, and 250 basis points are 2.5%. It is easier to talk about 30 basis points than “point three of one per cent”.
Bonds	Debt instruments issued by government, multinational companies, banks, multilateral development banks and corporates. Interest is paid by the issuer to the bond holder at regular pre-agreed periods. The repayment date of the principal is set at the outset.
Capital Expenditure	Spending on the purchase, major repair, or improvement of assets eg buildings and vehicles
Capital Financing Requirement (CFR)	Calculated in accordance with government regulations, the CFR represents the amount of Capital Expenditure that it has incurred over the years and which has not yet been funded from capital receipts, grants or other forms of income. It represents the Council’s underlying need to borrow.
Chartered Institute of Public Finance and Accountancy (CIPFA)	CIPFA is one of the leading professional accountancy bodies in the UK and the only one that specialises in the public services. It is responsible for the education and training of professional accountants and for their regulation through the setting and monitoring of professional standards. CIPFA has responsibility for setting accounting standards for local government.
Counterparty	Organisation with which the Council makes an investment
Credit Default Swaps	CDS are a financial instrument for swapping the risk of debt default and are effectively an insurance premium. Local authorities do not trade in CDS but trends in CDS prices are monitored as an indicator of relative confidence about the credit risk of counterparties.
Credit Rating	A credit rating is an independent assessment of the credit quality of an institution made by an organisation known as a rating agency. The rating agencies take many factors into consideration when forming their view of the likelihood that an institution will default on their obligations, including the institution’s willingness and ability to repay. The ratings awarded typically cover the short term outlook, the long term outlook, as well as an

	assessment of the extent to which the parent company or the state will honour any obligations. The three main agencies providing credit rating services are Fitch Ratings, Moody's and Standard and Poor's.
Fixed Deposits	Loans to institutions which are for a fixed period at a fixed rate of interest
Gilts	These are issued by the UK government in order to finance public expenditure. Gilts are generally issued for set periods and pay a fixed rate of interest. During the life of a gilt it will be traded at price decided in the market.
Housing Revenue Account (HRA)	There is a statutory requirement for local authorities to account separately for expenditure incurred and income received in respect of the dwellings that they own and manage.
Internal Borrowing	The temporary use of surplus cash which would otherwise be invested, as an alternative to borrowing from the PWLB or a bank in order to meet the cost of capital expenditure.
Lenders' Option Borrower's Option (LOBO)	A long term loan with a fixed interest rate. On pre-determined dates (eg every 5 years) the lender can propose or impose a new fixed rate for the remaining term of the loan and the borrower has the 'option' to either accept the new fixed rate or repay the loan.
LIBID	The rate of interest at which first-class banks in London will bid for deposit funds
Minimum Revenue Provision (MRP)	The minimum amount which must be charged to an authority's revenue account each year and set aside as provision for the repayment of debt.
Operational boundary	This is the most likely, prudent view of the level of gross external indebtedness. A temporary breach of the operational boundary is not significant.
Prudential Code/Prudential Indicators	The level of capital expenditure by local authorities is not rationed by central government. Instead the level is set by local authorities, providing it is within the limits of affordability and prudence they set themselves. The Prudential Code sets out the indicators to be used and the factors to be taken into account when setting these limits
Public Works Loan Board (PWLB)	A central government agency which provides long- and medium-term loans to local authorities at interest rates only slightly higher than those at which the Government itself can borrow.
Treasury Management Strategy Statement (TMSS)	Approved each year, this document sets out the strategy that the Council will follow in respect of investments and financing both in the forthcoming financial year and the following two years.

Appendix 2

Financial Performance Quarter 2 – Service details

	Qtr 2 Profiled Budget £'000	Qtr 2 actual £'000	Qtr 2 variance £'000
Service Delivery			
Housing and Environment			
: Regulatory Services - Licensing	(100)	(79)	21
: Regulatory Services - Public Health	39	31	(8)
: Regulatory Services - Food Safety	1	2	1
: Regulatory Services - Environmental Protection	13	26	13
: Regulatory Services - Health and Safety	1	0	(1)
: Regulatory Services - Port Health	1	2	1
: Community Safety	5	(20)	(25)
: Emergency Planning	21	21	0
: Homelessness	117	87	(30)
: Housing Strategy, Enabling and Advice	10	6	(4)
: Private Sector Housing Renewal	6	2	(4)
: Salaries, management, admin costs	1,405	1,215	(190)
Sub-total	1,519	1,293	(226)
Planning and Revenues			
: Building Control	(169)	(119)	50
: Coast Protection	13	0	(13)
: Flood Defence	68	72	4
: Development Control	(373)	(501)	(128)
: Street Naming	4	4	0
: Regulatory Services - Environmental Protection	(65)	(65)	0
: Council Tax Support Scheme Mgt	0	0	0
: Local Tax Collection - Council Tax	72	70	(2)
: Local Tax Collection - Business Rates	4	1	(3)
: Housing Benefit Administration	43	27	(16)
: Housing Benefit	(4,733)	(4,732)	1
: Salaries, management, admin costs	1,003	834	(169)
Sub-total	(4,133)	(4,409)	(276)
Customer Service			
: Regulatory Services - Animal and Pest Control	9	1	(8)
: Cemeteries	(7)	(6)	1
: Open Spaces	183	29	(154)
: Sports and Playing Fields	130	122	(8)
: Vehicle Workshop	(56)	51	107
: Internal Corporate Support Unit	77	98	21
: Salaries, management, admin costs	626	603	(24)
Sub-total	962	898	(64)

	Qtr 2 Profiled Budget £'000	Qtr 2 actual £'000	Qtr 2 variance £'000
Waste and Recycling			
: Recycling	412	512	100
: Waste Collection	511	450	(61)
: Street Cleansing	320	297	(23)
: Management and administration	143	112	(31)
: Robinson Road facility	59	51	(8)
Sub-total	1,445	1,422	(23)
Service Delivery Total	**(207)**	**(796)**	**(589)**
Business Strategy and Development			
Business Strategy and Performance			
: Voluntary Sector Support	99	102	3
: Print Plus service	(13)	13	26
: Salaries, management, admin costs	224	211	(13)
Sub-total	310	326	16
Regeneration and Investment			
: Tourism	76	98	22
: Culture and Heritage: Arts Development	(2)	0	2
: Economic Development	239	71	(168)
: Newhaven Enterprise Centre	(66)	(53)	13
: Salaries, management, admin costs	144	115	(29)
Sub-total	391	231	(160)
Strategic Policy			
: Planning Policy	25	(5)	(30)
: Planning Policy - Conservation	0	0	0
: Salaries, management, admin costs	220	194	(26)
Sub-total	245	189	(56)
Business Strategy and Development total	**946**	**746**	**(200)**
Corporate Services			
Property and Facilities			
: Investment Properties	(67)	(99)	(32)
: Industrial Estates	(332)	(343)	(11)
: Property Portfolio/Regeneration	52	82	30
: Public Conveniences	124	116	(8)
: Culture and Heritage - Newhaven Fort	58	71	13
: Indoor Leisure - Wave	308	280	(28)

	Qtr 2 Profiled Budget £'000	Qtr 2 actual £'000	Qtr 2 variance £'000
: Car Parking	(106)	(120)	(14)
: Office Accommodation	312	277	(35)
: Salaries, management, admin costs	160	178	18
Sub-total	509	442	(67)
Legal Services	225	267	42
Democratic Services			
: Democratic Representation	147	123	(24)
: Electoral Registration	56	26	(30)
: Elections - LDC	79	99	20
: Elections - other	0	12	12
: Local Land Charges	(11)	(73)	(62)
: Salaries, management, admin costs	156	157	1
Sub-total	427	344	(83)
Human Resources			
: Recruitment and Training	59	34	(25)
: HR service	179	180	1
Sub-total	238	214	(24)
Information Technology	720	812	92
Finance			
: Treasury Management	21	17	(4)
: Salaries, management, admin costs	370	327	(43)
Sub-total	391	344	(47)
Audit, Fraud and Procurement	134	136	2
Corporate Services Total	**2,644**	**2,558**	**(86)**
Corporate Strategy and Programmes			
: Corporate Management	117	172	55
: Organisational Development	0	46	46
: Salaries, management, admin costs	302	332	30
Corporate Strategy and Programmes total	**419**	**550**	**131**
Financing, interest, grants, etc			
Contributions to the HRA re shared items	0	0	0
Interest payments and receipts	(39)	(42)	(3)

	Qtr 2 Profiled Budget £'000	Qtr 2 actual £'000	Qtr 2 variance £'000
Town and Parish Council grant	118	119	1
Contributions to/from Reserves	0	0	0
Service Priority budget and savings target	(141)	0	141
Pensions accounting	42	76	34
Provision for Debt Repayment	0	0	0
Government Grants	(1,830)	(1,835)	(5)
Council Tax	0	0	0
Retained Business Rates	0	0	0
Use of Balance	0	0	0
Total	**(1,850)**	**(1,682)**	**168**
Central Support Service recharges	**(59)**	**(76)**	**(17)**
Housing Revenue Account			
Rent income	(7,733)	(7,739)	(6)
Charges for Services	(82)	(149)	(67)
Contributions towards expenditure	(21)	(21)	0
Community Amenities Contribution	0	0	0
Supervision and Management	151	97	(54)
Special Services	523	443	(80)
Repairs and Maintenance	1,607	1,618	11
Rents, rates, etc	133	135	2
Provision for irrecoverable debts	0	0	0
Capital accounting	0	0	0
Interest payments and receipts	864	849	(15)
Depreciation	0	0	0
Capital Programme funding	0	0	0
Transfer to/from HRA Balance	0	0	0
Total HRA	**(4,558)**	**(4,767)**	**(209)**
TOTAL	**(2,665)**	**(3,467)**	**(802)**