

**WEST OXFORDSHIRE DISTRICT COUNCIL**  
**FINANCE AND MANAGEMENT OVERVIEW AND SCRUTINY COMMITTEE**  
**2 DECEMBER 2015**

**TREASURY MANAGEMENT ACTIVITY AND PERFORMANCE 2015/16**

**REPORT OF GO SHARED SERVICE HEAD OF FINANCE**

**(Contact: Paul Stuart: - Tel (01993) 861171)**

**1. PURPOSE**

To advise members of treasury management activity and the performance of internal and external fund managers for the period 1 April 2015 – 31<sup>st</sup> October 2015.

**2. RECOMMENDATIONS**

That treasury management and the performance of in-house and external Pooled Funds' activity for the period 1 April 2015 – 31 October 2015 are noted.

**3. BACKGROUND**

**Investment Portfolio Background**

- 3.1. The in- house investment balance amounted to £11.035m at 1 April 2015 inclusive of the long term loan to Hanover Housing Association. The average balance of investments for the period to 31<sup>st</sup> October 2015 rose to £16.990m in line with cash-flow forecasts for 2015/16.
- 3.2. Bonds purchased in 2013/14 (at a cost of £4.942m) were valued at £5.169m at 31<sup>st</sup> March 2015 and are now valued at £4.996m on 31<sup>st</sup> October 2015 based on current mid-prices. These bonds were acquired on a principle of holding to maturity.
- 3.3. The performance of all funds is continually monitored and compared against the 3 month LIBID rate which was 0.43% as at 31 October 2015.

**Investment Activity**

- 3.4. The guidance on Local Government Investment in England gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles.

Long term security of capital remains the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2015/16. New investments were made in line with policy as quoted in the Investment Strategy for 2015/16:

- AAA-rated Money Market Funds;
- Term Deposits with UK Banks and Building Societies systemically important to the UK banking system;
- Pooled funds (collective investment schemes) meeting the criteria in SI 2004 No 534 and subsequent amendments.

Counterparty credit quality was assessed and monitored with reference to Credit Ratings (the Council's minimum long-term counterparty rating of A- (or equivalent) across rating agencies Fitch, S&P and Moody's); credit default swaps; financial statements, information on potential government support and reports in the quality financial press

- 3.5. Given the increasing risk and continued low returns from short-term unsecured bank investments, the Authority has a well-balanced and diversified investment portfolio but needs to consider other investment vehicles to counteract risks from changes to bail-in legislation.

The cash investments outstanding at 31 October 2015 are detailed in Appendix A.

### Investment Performance

- 3.6 Performance Achieved for the period (excluding outstanding Icelandic investments) is shown below:-

<b>Performance of Fund I April 2015 to 31 October 2015 (annualised returns)</b>	<b>In-House</b>	<b>Bonds</b>
Net Return	1.38%	3.76%

- 3.7 In-house investment achieved a net return of 1.38% which is 0.95% above the 3 month LIBID rate. The outperformance is due to the £5m loan to Hanover Housing Association at a rate of 3.35% and a number of Certificate of Deposits (CD's) with Standard Chartered at the beginning of year with an average rate of 0.71% and a small pick-up in short term rates (3-6 months) over the same period. However it should be noted in-house investments are largely constrained by cash flow commitments such as precept payments, benefit pay-out as well as the capital programme requirements.
- 3.8 During August 2015, for technical accounting reasons, after consultation with Arlingclose officers switched all of the Pooled Funds from accumulation funds to income share class. This change allows regular income dividend payments to the Council, (monthly, quarterly or half yearly) as revenue. An estimate for the year's return for these dividends is approximately £180,000. The table below shows the current value of the Pooled Funds but does not reflect the expected dividend.
- 3.9 The table shows the current valuations after a number of very difficult months in markets, particularly in August and September, which saw equity markets and bond yields fall led by the stock market turmoil in China. Indices have not recovered to their previous levels but some improvement has been seen on some of the Funds listed above. The impact on the market is reflected in the Fund Values shown above and Appendix B to the report provides detailed movement in price and value of Funds since the initial investments were made. It should be noted the fall in Fund Value will only occur at the point of selling the investment.

## Pooled Funds Portfolio

	Initial Investment	1 April Fund Value	31 October Fund Value	Unrealised Gain / (Loss) for 2015/16	Unrealised Gain / (Loss) to Initial Principal
	£	£	£	£	£
Insight LPF – Cash +	2,000,000	2,016,036	2,017,760	1,724	17,760
Payden & Rygel – Cash +	2,000,000	2,025,667	2,024,053	(1,614)	24,053
UBS – Bond / Equity	2,000,000	1,065,124	1,995,160	(69,964)	(4 840)
M&G Strategic – Bond	1,000,000	0	978,376	(21,624)	(21,624)
Aberdeen – Bond	2,000,000	3,830,882	1,815,819	(15,063)	(184,181)
Schroders – Equity	1,000,000	1,105,041	1,001,006	(104,035)	1,006
Threadneedle – Equity	1,000,000	1,121,811	1,080,399	(41,412)	80,399
M&G Global - Equity	1,000,000	1,075,050	965,237	(109,813)	(34,763)
October 2015	<b>12,000,000</b>	12,239,611	<b>11,877,810</b>	<b>(361,801)</b>	<b>(122,192)</b>
Previously Report- August			<b>11,851,388</b>	<b>(388,223)</b>	<b>(148,612)</b>

### Interest rate outlook

- 3.10 Arlingclose expectation for the first rise in the Bank Rate remains the second calendar quarter of 2016 as seen in the table below. The pace of interest rate rises will be gradual and the extent of rises limited. For the post-crisis UK economy it is likely to see lower rates than the previous norm with rates between 2% and 3%. 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.
- 3.11 The weak global environment and resulting low inflation expectations are likely to dampen long term interest rates. 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
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
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
Downside risk				-0.25	-0.25	-0.50	-0.50	-0.75	-0.75	-1.00	-1.00	-1.00

### **Bail-in Risk- Reverse Purchase Agreements ('Repos') and Covered Bonds**

- 3.12 As mentioned in 3.5 above changes to banking legislation now mean that the Council is exposed to credit risk alongside equity holders.
- 3.13 Bail-in allows regulatory authorities to keep a failing bank open for essential business, but passes the cost of that failure onto investors instead of taxpayers via a bail-out. Previously, bondholders and depositors would only lose money if a bank entered insolvency. Under a bail-in regime, the regulator can apply a 'haircut' to bonds and deposits to reduce a bank's liabilities and therefore increase its equity capital, without interrupting the provision of current accounts, mortgages and business loans.
- 3.14 Given the practicalities of day to day cash management, it is unlikely the Council will be able to avoid making any unsecured investments in banks and building societies. Money Market Funds provide an instant access alternative, but since they mostly invest in unsecured certificates of deposit issued by banks, the only risk reduction is through diversification. Government MMFs, which mostly invest in treasury bills and repurchase agreements (repos), are a low risk solution with consequent returns after fees typically being very low.
- 3.15 Reverse Purchase Agreements ('Repos') provide a secured way for an investor to make a loan to a bank. Legally there are two linked transactions: the sale of bonds by the bank, normally valued higher e.g. 105%, of the principal amount of the loan agreement. Consequently, the bank has a forward agreement to repurchase them on maturity, but if the bank defaults, the investor would retain ownership of the bond; the economic effect is a short-term loan by the investor to a bank and they are accounted for as such.
- 3.16 As reverse repurchase agreements with banks are exempt from bail-in, they make prudent investment sense for local authorities whose investments with banks such as call accounts, term deposits and certificates of deposit are as unsecured investors and subject to bail-in. Covered bonds offer similar suitable vehicles.
- 3.17 Working with Arlingclose officers included both Repo's and Covered Bonds within the strategy last year and as a consequence officers will, as the banking legislations comes into force, move bank deposits to Repo's and Covered Bonds. Currently repo rates for short-dated lending (1-6 months) are very close to those for unsecured investments with banks (deposits/CDs) and therefore on a risk/return basis provide exceptional value.

#### 4. FINANCIAL IMPLICATIONS

- 4.1. The original investment interest budget for 2015/16 was set at £550,000 which was based on an average balance of £32.9 million from all the different type of investments (e.g. fixed term deposits, pooled funds, bonds) achieving an overall average return of 1.67%. The breakdown of the budget and a comparative forecast is as follows:

	2015/16 Budget (£)	2015/16 Forecast (£)
Pooled Fund Managers	120,000	180,000
In-House Investments	72,500	70,000
Hanover Housing Assoc	167,500	167,500
Bonds	190,000	188,000
Total	550,000	605,500

- 4.2. At present there are fluctuations within Pooled Funds and Bond valuations, however officers are comfortable the overall budget will be achieved this financial year and it is important to look through temporary capital value fluctuations.

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GO Shared Service Head of Finance

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Date: 20 November 2015

Background Papers

Valuation 31<sup>st</sup> October 2015 – Pooled Funds & Bonds

In – House investment as at 31<sup>st</sup> October 2015

## SCHEDULE OF CASH INVESTMENTS OUTSTANDING AT 31 October 2015

NAME OF COUNTERPARTY	VALUE DATE	NOMINAL AMOUNT (£)	MATURITY DATE	RATE OF INTEREST	Long Term	Fitch Credit Rating		
						Short Term	Viability	Support
<b>IN HOUSE MANAGEMENT</b>								
Hanover Housing Association	24.07.13	5,000,000	24.07.18	3.35%	A	FI	a	5
Barclays	03.08.15	1,000,000	03.11.15	0.53%	A	FI	a	5
Lloyds	11.09.15	1,000,000	11.03.16	0.75%	A	FI	a	5
Standard Chartered	01.10.15	2,000,000	01.03.16	0.66%	A	FI	a	5
Nationwide	02.10.15	1,000,000	02.03.16	0.60%	A	FI	a	5
Nationwide	09.10.15	1,000,000	09.02.16	0.56%	A	FI	a	5
Lloyds	12.10.15	1,000,000	12.02.16	0.60%	A	FI	a	5
Lloyds	13.10.15	2,000,000	14.03.16	0.65%	A	FI	a	5
Goldman Sachs MMF	31.10.15	2,020,000		0.45%	AAAmf			
Invesco AIM MMF	31.10.15	3,200,000		0.43%	AAAmf			
<b>TOTAL IN-HOUSE INVESTMENTS</b>		<b>19,220,000</b>						
<b>ICELANDIC BANK DEPOSITS</b>								
Glitnir Escrow	27.06.07	236,166		3.71%				
Kaupthing Singer Friedlander	02.07.07	159,144		-				
Glitnir Escrow (Tradition)	31.08.07	538,041		3.71%				
<b>TOTAL ICELANDIC DEPOSITS</b>		<b>933,351</b>						

## POOLED FUND &amp; BONDS PORTFOLIO VALUATION AT 31 OCTOBER 2015

	Insight Liquidity Plus Fund - Share Class 3		Payden & Rygel Sterling Reserve Fund - Accumulation		UBS Multi Asset Income Fund - L Class Accumulation Gross	
Transaction Ref	33544		AA1771001		0000486436	
Date of purchase	31/03/2014		28/03/2014		28/03/2014	
Number of units/shares	1,520,045.601		189,845.181		1,866,019.780	
Purchase Price £	1.31575		10.5349		0.536	
Initial investment 2013/14 £	2,000,000		2,000,000		1,000,000	
Initial investment 2014/15						
<b><u>Transactions 2015/16</u></b>						
Number of units/shares					1,747,030.049	
Purchase/Sale Price £					0.5724 1,000,000	
Apr-15	1.3269	2,016,979	10.6679	2,025,249	0.57210	1,067,550
May-15	1.3275	2,017,921	10.6759	2,026,768	0.57240	2,068,110
Jun-15	1.3280	2,018,545	10.6693	2,025,515	0.56170	2,029,450
Jul-15	1.3279	2,018,453	10.6679	2,025,249	0.56550	2,043,180
Transaction Ref	A30R682650459433		1474		0000552409	
Date of switch	17/08/2015		07/08/2015		07/08/2015	
Ticker/Number of income shares	<b>INLIQP5</b>	2,051,799.720	<b>PAYSRSD</b>	200,707.339	<b>UMAIGLI</b>	3,928,254.420
Price of income shares /Value	0.98397	<b>2,018,909</b>	10.0951	<b>2,026,161</b>	0.5204	<b>2,044,264</b>
Aug-15	0.9841	2,019,074	10.0996	2,027,064	0.5069	1,991,232
Sep-15	0.9838	2,018,643	10.0840	2,023,933	0.4977	1,955,092
Oct-15	0.9834	2,017,760	10.0846	2,024,053	0.5079	1,995,160
Variance to initial investment	<b>17,760</b>		<b>24,053</b>		<b>(4,840)</b>	
	<i>Div payable monthly</i>		<i>Div payable quarterly</i>		<i>Div payable quarterly</i>	

	<i>Aberdeen (SWIP) Absolute Return Bond Fund - D Class Accumulation</i>	<i>M&amp;G Strategic Corporate Bond Fund I Class Accumulation</i>	<i>Schroders Income Maximiser Fund - Z Class Accumulation</i>
Transaction Ref	P3B/003072Z/1		0016426876
Date of purchase	25/03/2014		08/04/2014
Number of units/shares	3,676,470.588		1,509,206.160
Purchase Price £	1.088		0.6626
Initial investment 2013/14 £	4,000,000		
Initial investment 2014/15			1,000,000
<b><u>Transactions 2015/16</u></b>			
Number of units/shares	1,917,545.542	86,261.182	
Purchase/Sale Price £	1.043 (2,000,000)	11.59270 1,000,000	
Apr-15	1.0520 1,850,389		0.7375 1,113,040
May-15	1.0552 1,856,018	11.6181 1,002,191	0.7506 1,132,810
Jun-15	1.0570 1,859,184	11.4077 984,042	0.7175 1,082,855
Jul-15	1.0510 1,848,630	11.4784 990,140	0.7184 1,084,214
Transaction Ref	0055105862	0236981915	00184184431
Date of switch	07/08/2015	10/08/2015	06/08/2015
Ticker/Number of income shares	<b>ABARBII</b> 1,884,216.379	<b>MGSCBII</b> 93,089.085	<b>SCHIMZI</b> 2,013,286.550
Price of income shares /Value	0.9799 1,846,344	10.6691 993,177	0.5470 1,101,268
Aug-15	0.9751 1,837,299	10.5952 986,297	0.5065 1,019,730
Sep-15	0.9650 1,818,269	10.5020 977,622	0.4791 964,566
Oct-15	0.9637 1,815,819	10.5101 978,376	0.4972 1,001,006
Variance to initial investment	(97,891)	(21,624)	1,006
	<i>Div payable semi-annually</i>	<i>Div payable quarterly</i>	<i>Div payable quarterly</i>



	Threadneedle Global Equity Income Fund - Z Class Accumulation Net		M&G Global Dividend Fund - Class I Accumulation		
Transaction Ref	0006673718		0226768331		
Date of purchase	01/04/2014		26/03/2014		
Number of units/shares	973,709.835		489,993.898		
Purchase Price £	1.0270		2.041		
Initial investment 2013/14 £			1,000,000		
Initial investment 2014/15	1,000,000				
<b><u>Transactions</u></b>					
<b><u>2015/16</u></b>					
Number of units/shares					
Purchase/Sale Price £					
	Apr-15	1.1430	1,112,950	2.2121	1,083,916
	May-15	1.1608	1,130,282	2.2297	1,092,539
	Jun-15	1.0877	1,059,104	2.1000	1,028,987
	Jul-15	1.0938	1,065,044	2.0796	1,018,991
Transaction Ref	0010119872		023697193		
Date of switch	07/08/2015		10/08/2015		
Ticker/Number of income shares	THGQZNI 907,898.550		MGGDIIG 616,095.772		
Price of income shares /Value	1.1792 1,070,594		1.6271 1,002,449		
	Aug-15	1.1291 1,025,108	1.5348	945,584	
	Sep-15	1.1087 1,006,587	1.4678	904,305	
	Oct-15	1.1900 1,080,399	1.5667	965,237	
Variance to initial investment	80,399		(34,763)		
	<i>Div payable quarterly</i>		<i>Div payable quarterly</i>		