MEETING	**PENSIONS COMMITTEE**
DATE	**8 SEPTEMBER 2015**
PURPOSE	**CIPFA'S CODE OF PRACTICE REQUIRES THAT A REPORT BE PRODUCED ON THE RESULTS OF THE COUNCIL'S ACTUAL TREASURY MANAGEMENT ON BEHALF OF THE PENSION FUND.**
TITLE	**TREASURY MANAGEMENT 2014/15**
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1. Introduction and Background

CIPFA's revised Code of Practice on Treasury Management was adopted by the Council on 1st March 2011 and the Council fully complies with its requirements. The Code requires that I report on the results of the Council's actual treasury management in the previous financial year against expectations.

In accordance with the Welsh Assembly Government's Statutory Guidance on Local Government Investments, which requires an authority to produce an Annual Investment Strategy, it was considered best practice for the Gwynedd Pension Fund (the "Fund") to adopt Gwynedd Council's Treasury Management Strategy Statement (TMSS) for 2014/15, as amended for the purpose of the Pension Fund. The Pensions Committee approved the TMSS at its meeting on 17 March 2014. As a result, I am required to report on the results of the actual treasury management in 2014/15 against expectations.

2. Investment Activity

The Welsh Assembly Government's (WAG's) revised Investment Guidance came into effect on 1st April 2010 and reiterated the need to focus on security and liquidity, rather than yield. It also recommended that strategies include details of assessing credit risk, reasons for borrowing in advance of need and the use of treasury advisers.

Pension Fund Balances	Balance on 31/03/2014 £m	Balance on 31/03/2015 £m
Balances	10.7	13.4

As requested by the Pensions Committee on 17 March 2014, the pension fund's money was pooled with the Council's general cashflow. As agreed at the Pensions Committee on 24 March 2015 this arrangement continues in 2015/16. Interest rates are still very low but there is no reason to change this decision.

The table below shows a summary of where this pooled money was invested during 2014/15.

Investments	Balance on 01/04/14 £’000	Investments Made £’000	Maturities/ Investments Sold £’000	Revalue to Fair Value £’000	Balance on 31/03/15 £’000	Average Rate %
Call Accounts with Banks with ratings of A- or higher - short term	20,825	157,650	(160,055)	0	18,420	0.47
Investments with Banks and Building Societies with ratings of A- or higher - short term	27,000	52,597	(42,595)	0	37,002	0.78
Building Society Covered Bond – long term	0	1,088	0	33	1,121	0.45
Money Market Funds	0	89,796	(89,796)	0	0	2.09
TOTAL INVESTMENTS	**47,825**	**301,131**	**(292,446)**	**33**	**56,543**	
Increase/ (Decrease) in Investments £m					8,718	

Security of capital has remained the Authority’s main investment objective. This was maintained by following the Authority’s counterparty policy as set out in its Treasury Management Strategy Statement for 2014/15.

Counterparty credit quality was assessed and monitored with reference to credit ratings (the Authority’s minimum long-term counterparty rating was A- across rating agencies Fitch, S&P and Moody’s), credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

Credit Risk
Counterparty credit quality as measured by credit ratings is summarised below:

Date	Value Weighted Average Credit Risk Score	Value Weighted Average Credit Rating	Time Weighted Average Credit Risk Score	Time Weighted Average Credit Rating	Average Life (days)
31/03/2014	5.69	A	5.80	A	102
30/06/2014	5.19	A+	5.12	A+	139
30/09/2014	5.01	A+	3.21	AA	118
31/12/2014	5.39	A+	3.49	AA	148
31/03/2015	5.24	A+	3.62	AA-	64

Scoring:
-Value weighted average reflects the credit quality of investments according to the size of the deposit
-Time weighted average reflects the credit quality of investments according to the maturity of the deposit
-AAA = highest credit quality = 1
- D = lowest credit quality = 26
-Aim = A- or higher credit rating, with a score of 7 or lower, to reflect current investment approach with main focus on security

Counterparty Update

The European Parliament approved the EU Bank Recovery and Resolution Directive (BRRD) on April 15, 2014. Taking the view that potential extraordinary government support available to banks' senior unsecured bondholders will likely diminish, over 2014-15 Moody's revised the Outlook of several UK and EU banks from Stable to Negative (note, this is not the same as a rating review negative) and S&P placed the ratings of UK and German banks on Credit Watch with negative implications, following these countries' early adoption of the bail-in regime in the BRRD.

S&P also revised the Outlook for major Canadian banks to negative following the government's announcement of a potential bail-in policy framework.

The Bank of England published its approach to bank resolution which gave an indication of how the reduction of a failing bank's liabilities might work in practice. The Bank of England will act if, in its opinion, a bank is failing, or is likely to fail, and there is not likely to be a successful private sector solution such as a takeover or share issue; a bank does not need to be technically insolvent (with liabilities exceeding assets) before regulatory intervention such as a bail-in takes place.

The combined effect of the BRRD and the UK's Deposit Guarantee Scheme Directive (DGSD) is to promote deposits of individuals and SMEs above those of public authorities, large corporates and financial institutions. Other EU countries, and eventually all other developed countries, are expected to adopt similar approaches in due course.

In December the Bank's Prudential Regulation Authority (PRA) stress tested eight UK financial institutions to assess their resilience to a very severe housing market shock and to a sharp rise in interest rates and address the risks to the UK's financial stability. Institutions which 'passed' the tests but would be at risk in the event of a 'severe economic downturn' were Lloyds Banking Group and Royal Bank of Scotland. Lloyds Banking Group, [whose constituent banks are on the Authority's lending list], is taking measures to augment capital and the PRA does not require the group to submit a revised capital plan. RBS, which is not on the Authority's lending list for investments, has updated plans to issue additional Tier 1 capital. The Co-operative Bank failed the test.

The European Central Bank also published the results of the Asset Quality Review (AQR) and stress tests, based on December 2013 data. 25 European banks failed the test, falling short of the required threshold capital by approximately €25bn (£20bn) in total – none of the failed banks featured on the Authority's lending list.

In October following sharp movements in market signals driven by deteriorating global growth prospects, especially in the Eurozone, Arlingclose advised a reduction in investment duration limits for unsecured bank and building society investments to counter the risk of another full-blown Eurozone crisis. Duration for new unsecured investments with some UK institutions was further reduced to 100 days in February 2015.

The outlawing of bail-outs, the introduction of bail-ins, and the preference being given to large numbers of depositors other than local authorities, means that the risks of making unsecured deposits rose relative to other investment options. The Authority therefore has started to use secured investment options or diversified alternatives such as covered bonds, in addition to unsecured bank and building society deposits. Deposits were generally made over short periods in order to reduce the risk. Use of secured options including non-bank investments and pooled funds as well as covered bonds is likely to increase in order to reduce the risk of default.

Update on Investment with Heritable Bank

The authority has now recovered 94% of its investment in Heritable Bank. It is likely that further distributions will be received and that the full amount should be recovered. The timing of future distributions is unclear and depends on settlement of the ongoing court case. Notice that a dividend will be paid in August 2015 has been received but the amount is not yet known.

3. Recommendation

The Pensions Committee is asked to receive the report on investment of the Fund's cash, pooled with the Council's cash, in 2014/15 for information.

APPENDIX

Credit Score Analysis

Scoring:

Long-Term Credit Rating	**Score**
AAA	1
AA+	2
AA	3
AA-	4
A+	5
A	6
A-	7
BBB+	8
BBB	9
BBB-	10

The value weighted average reflects the credit quality of investments according to the size of the deposit. The time weighted average reflects the credit quality of investments according to the maturity of the deposit

The Authority aimed to achieve a score of 7 or lower, to reflect the Authority's overriding priority of security of monies invested and the minimum credit rating threshold of A- for investment counterparties.