PLYMOUTH CITY COUNCIL

Subject:	Treasury Management Report – The Impact of Leaving the European Union
Committee:	Audit Committee
Date:	8 December 2016
Cabinet Member:	Councillor Darcy
CMT Member:	Andrew Hardingham (Assistant Director for Finance)
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Ref:	FIN/CF
Key Decision:	No
Part:	I

Purpose of the report:

The report is to provide a commentary on the effects on Treasury Management caused by the UK's decision to leave the European Union.
The report gives a general update on the changes in the economy and the markets and how these have affected the Council's Treasury Management.

The Council's Corporate Plan 2016/19

Effective financial management is fundamental to the delivery of corporate improvement priorities. Treasury Management activity has a significant impact on the Council's activity both in revenue budget terms and capital investment and is a key factor in facilitating the delivery against a number of corporate priorities.

Implications for Medium Term Financial Plan and Resource Implications: Including finance, human, IT and land

The changes in Treasury Management will have implications on Treasury Management budget. The income on the Council's investment has fallen but this will be partially compensated by the falling cost of borrowing.

Other Implications: e.g. Child Poverty, Community Safety, Health and Safety and Risk Management:

N/A

Equality and Diversity

Has an Equality Impact Assessment been undertaken? No

1) Recommendations and Reasons for recommended action:

The Audit Committee to note the report.

Alternative options considered and rejected:

None

Published work / information:

Background papers: None

None

Sign off:

		Leg		Mon Off		HR		Assets		IT		Strat Proc	
Originating SMT Member – Andrew Hardingham													
Has the Cabinet Member(s) agreed the contents of the report? Yes													

Treasury Management Report – The Impact of Leaving European Union – December 2016

Economic update from Treasury Management advisors Arlingclose

The major external influence on the Authority's treasury management strategy for 2017/18 will be the UK's progress in negotiating a smooth exit from the European Union.

Financial markets, wrong-footed by the referendum outcome, have since been weighed down by uncertainty over whether leaving the Union also means leaving the single market. Negotiations are expected to start once the UK formally triggers exit in early 2017 and last for at least two years.

Uncertainty over future economic prospects will therefore remain throughout 2017/18.

The fall and continuing weakness in sterling and the near doubling in the price of oil in 2016 have combined to drive inflation expectations higher.

The Bank of England is forecasting that Consumer Price Inflation will breach its 2% target in 2017. This will be the first time this has happened since late 2013. The Bank is expected to look through inflation overshoots over the course of 2017 when setting interest rates so as to avoid derailing the economy.

Initial post-referendum economic data showed that the feared collapse in business and consumer confidence had not immediately led to lower GDP growth.

The prospect of a leaving the single market has dented business confidence and resulted in a delay in new business investment. Unless counteracted by higher public spending or retail sales, a delay in new business investment will weaken economic growth in 2017/18.

Looking overseas, the US economy and its labour market are showing steady improvement. The market has priced in a high probability of the Federal Reserve increasing interest rates in December 2016.

The Eurozone meanwhile has continued to struggle with very low inflation and lack of momentum in growth, and the European Central Bank has left the door open for further quantitative easing.

The impact of political risk on financial markets remains significant over the next year.

Challenges have the potential for upsets. These include:

- Immigration
- The rise of populist, anti-establishment parties
- Negative interest rates which have resulted in savers being paid nothing or little for their frugal efforts
- The outcomes of Italy's referendum on its constitution (December 2016)
- The French presidential and general elections (April – June 2017)
- The German federal elections (August – October 2017)

PWLB **-** The government has confirmed plans to abolish the 223-year-old Public Works Loan Board and transfer its functions for lending to local authorities to the Treasury.

Interest Rate Forecast

The central case is for UK Bank Rate to remain at 0.25% during 2017/18. The Bank of England has, however, highlighted that excessive levels of inflation will not be tolerated for sustained periods.

Given this view and the current inflation outlook, further falls in the Bank Rate look less likely.

Autumn Statement Summary

Growth forecasts have been reduced by Office for Budget Responsibility. The Chancellor is borrowing to fund infrastructure. There are marginal taxation changes with the objective of securing a level playing field between different categories of employment.

Public borrowing/deficit/spending

- Borrowing is forecast to be £122bn higher in the period until 2021 than forecast in March's Budget
- Debt will rise from 84.2% of GDP last year to 87.3% this year, peaking at 90.2% in 2017-18
- Office for Budget Responsibility (OBR) forecasts borrowing of £68.2bn this year, then £59bn in 2017-18, £46.5bn in 2018-19, £21.9bn in 2019-20 and £20.7bn in 2020-21
- Public spending this year to be 40% of GDP - down from 45% in 2010
- Departmental spending plans set out in 2015 Spending Review to remain in place
- Government will meet commitments to protect budgets for key public services, defence, overseas aid and the pension "triple lock" until the end of this Parliament

The state of the economy

- OBR growth forecast upgraded to 2.1% in 2016 - from 2.0% - then downgraded to 1.4% in 2017, from 2.2%
- Forecast growth of 1.7% in 2018, 2.1% in 2019 and 2020 and 2% in 2021
- Government no longer seeking a budget surplus in 2019-20 - committed to returning public