

**REPORT TO: POLICY AND RESOURCES COMMITTEE ON 2 FEBRUARY 2010**

**SUBJECT: TREASURY MANAGEMENT – MONITORING REPORT FOR THE PERIOD 1 OCTOBER 2009 TO 31 DECEMBER 2009**

**BY: CHIEF FINANCIAL OFFICER**

**1. REASON FOR REPORT**

- 1.1 To advise Committee on matters relating to the Treasury Management function for the third quarter of the 2009/10 financial year.
- 1.2 This report is submitted to Committee in terms of Section A (3) of the Council's Administrative Scheme relating to Treasury Management.

**2. RECOMMENDATION**

- 2.1 It is recommended that the Committee consider the contents of this Report.
- 2.2 Approve The Revised Counterparty List detailed in Appendix 3.

**3. BACKGROUND**

- 3.1 In terms of the Council's Financial Regulations, a Monitoring Report requires to be submitted quarterly to the Policy and Resources Committee detailing the movements in the debt portfolio.
- 3.2 The Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector. All treasury management activities are carried out in accordance with the Code.

**Economic Background**

- 3.3 The Council's Treasury Advisers forecast that the first increase in the bank base rate will be during the quarter ending September 2010. Thereafter, the base rate is expected to reach 4.5% by the end of March 2013. The PWLB 50 year rate is expected to steadily increase to 5.45% by the end of 2012 due to huge gilt issuance by the Government, the reversal of quantitative easing and investor concerns over inflation.

- 3.4 There is considerable uncertainty in all economic forecasts due to the difficulties of predicting the timing and amounts of quantitative easing reversal, the fiscal effect of a general election, speed of recovery of banks profitability and balance sheet positions, changes in the consumer saving ratio and rebalancing of the UK economy in terms of export and import.

### **Long Term Borrowing**

- 3.5 The total long term debt outstanding at 31 December 2009 was £123.3 million and the average length of that debt was 41.03 years with an average interest rate of 5.86%.
- 3.6 The debt outstanding comprises PWLB fixed rate loans and market loans. The periods for repayment range from 10.5 to 67 years. The debt is split as follows: -

|              | <b>£m</b>    | <b>Average Rate (%)</b> | <b>Proportion of Total Debt (%)</b> |
|--------------|--------------|-------------------------|-------------------------------------|
| PWLB         | 89.9         | 6.36                    | 72.9                                |
| Market Loans | 33.4         | 4.51                    | 27.1                                |
| <b>TOTAL</b> | <b>123.3</b> | <b>5.86</b>             | <b>100.0</b>                        |

- 3.7 The Public Works Loan Board (PWLB) is a statutory body operating within The UK Debt Management Office, which is an executive agency of H.M.Treasury. PWLB's function is to lend money from the National Loans Fund to Local Authorities and other prescribed bodies, and to collect the repayments. The Market Loans are held by Barclays Bank (£23.3million) and EuroHypo Bank, Luxemburg (£10.1million). A profile of long-term debt repayments for the current debt portfolio is shown as **APPENDIX 1**.

### **Short Term Borrowing**

- 3.8 During the quarter a total of £8.3 million of temporary borrowing was undertaken at an average rate of 0.34%. The value of temporary borrowing ranged from £3.0million to £11.3million. As at 31 December 2009 temporary borrowing of £9.3 million was held.

### **Investments**

- 3.9 During the period 1 October to 31 December 2009, surplus funds of between £30,000 and £9.495 million at any one time were deposited in a Call Account with the Council's Bankers, Bank of Scotland, at a rate of 0.85%.
- 3.10 As at 31 December 2009, £2.145 million was held on deposit in the Call Account with the Council's Bankers. The Council also has £2 million on deposit with the Icelandic bank, Landsbanki. That bank is in receivership and the deposit is currently frozen.

- 3.10.1 Following submission of formal claims to Landsbanki on 30 October, the Landsbanki Winding-up Board (WUB) has confirmed it has accepted all local authority claims as priority claims, subject to some modifications around the penalty interest applicable to each claim. The Council's Legal advisers are working with advisers for other depositor countries to raise objections to these modifications, but are pleased that the WUB has accepted the priority status of the claims. However, as anticipated, we understand that other, non-priority creditors of Landsbanki (specifically bond-holders and a range of international banks) have filed objections to every decision by the WUB to accept a claim as having priority status.
- 3.10.2 The deadline for submitting written statements in response to objections that have been filed is 10 January 2010, and our advisers are liaising with the Landsbanki WUB to clarify whether we can comment on objections filed by others. Following the 10 January deadline, we understand that the WUB will initiate a process of mediation, after which outstanding objections will be filed by the WUB to the courts. This means that legal action over the depositor preference issue is likely to begin in Spring 2010.
- 3.11 Performance of investments is measured against the benchmark of the average 7 day London Interbank Bid Rate (LIBID). During the period the average rate achieved by the Council was 0.85% and the average LIBID rate was 0.38%.

### **Counterparty List**

- 3.12 The Chief Financial Officer maintains a Counterparty list which is reviewed daily and complies with the criteria detailed in para 3.13.1. The criteria are regularly reviewed and any revision is submitted to Committee for approval as necessary.
- 3.13 The Council uses Fitch credit ratings to derive its Counterparty criteria. Where a Counterparty does not have a Fitch rating, an equivalent rating is used. All credit ratings are monitored daily and the Counterparty list is amended to reflect any changes.

3.13.1 The Council's current criteria are:

- **Banks** – the Council will use banks which have at least the following Fitch or equivalent ratings. (Further details of these ratings are shown in **APPENDIX 2**)
  - **Short Term – F1**
  - **Individual / Financial Strength – C**
  - **Support – 1**
- **Bank Subsidiary and Treasury Operations** – the Council will use these where the parent bank has the necessary ratings outlined above.
- **Building Societies** – the Council will include all Societies, which meet the ratings for banks outlined above.
- **UK Government** (Debt Management Office)
- **Local Authorities** (These bodies have a statutory duty to set Council Tax so that their budgets break even)

- 3.14 In addition to the Fitch Credit Ratings, the Council's Treasury Management Consultants provide a creditworthiness matrix to aid the assessment of risk involved in lending to individual counterparties. The Council's Counterparty List is constantly monitored in conjunction with this matrix.
- 3.15 The Counterparty List has been amended to reflect upgrades of Individual Ratings for Lloyds TSB, Bank of Scotland, Royal Bank of Scotland and Alliance & Leicester; the downgrade of Individual Rating for HSBC; change of name from Abbey National to Santander UK and the removal of Northern Rock from the list due to changes in the deposit guarantee arrangements which has resulted in Northern Rock falling below the minimum criteria. **(APPENDIX 3).**

### **The Prudential Code for Capital Finance in Local Authorities**

- 3.16 The Local Government (Scotland) Act 2003 requires the Council to undertake its treasury activities with regard to the Prudential Code for Capital Finance in Local Authorities.
- 3.17 The Code requires the Council to produce mandatory indicators aimed at assisting Members in ensuring that proposed capital investment levels and treasury management decisions satisfy the key requirements of affordability, prudence and sustainability. The Prudential Indicators for 2009/10 were approved by the Full Council on 12 February 2009. Performance against key Indicators for Treasury is shown below.

### **Treasury Prudential Indicators**

|                                                      | <b>Estimate<br/>2009/10<br/><br/>£ m</b> | <b>Actual<br/>2009/10<br/>to 31 Dec 2009<br/>£ m</b> |
|------------------------------------------------------|------------------------------------------|------------------------------------------------------|
| <b>Authorised limit for<br/>External Debt</b>        | 174,147                                  | 174,147                                              |
| <b>Operational Boundary for<br/>External Debt</b>    | 169,147                                  | 132,567                                              |
| <b>Upper Limit on Fixed<br/>Interest Exposure</b>    | 100                                      | 74.81                                                |
| <b>Upper Limit on Variable<br/>Interest Exposure</b> | 30                                       | 25.19                                                |

| <b>Maturity Structure</b> | <b>Lower</b> | <b>Upper</b> | <b>Actual to 31 Dec 2009</b> |
|---------------------------|--------------|--------------|------------------------------|
| Under 12 months           | 0%           | 15%          | 0%                           |
| 1 – 2 years               | 0%           | 50%          | 0%                           |
| 2 – 5 years               | 0%           | 50%          | 0%                           |
| 5 – 10 years              | 0%           | 75%          | 0%                           |
| 10 years & above          | 0%           | 100%         | 100%                         |

#### **4 SUMMARY OF IMPLICATIONS**

**(a) Single Outcome Agreement/Service Improvement Plan**

None.

**(b) Policy and Legal**

The Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Sector. All Treasury Management activities are carried out in accordance with the Code.

**(c) Resources (Financial, Risks, Staffing and Property)**

The Treasury Management Strategy for 2009/10 was based on close monitoring of the interest rate market with a view to making a sound long-term debt portfolio whilst minimising the Council's exposure to risk.

**(d) Consultations**

None.

#### **5. CONCLUSION**

**5.1 The Council's requirement for funds continues to be managed in accordance with the agreed Treasury Management strategy.**

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Background Papers:

Ref: AB/MW/LJC/725994/726004/583640/726007