

**REPORT TO: POLICY AND RESOURCES COMMITTEE ON 27 APRIL 2010**

**SUBJECT: TREASURY MANAGEMENT – MONITORING REPORT FOR THE PERIOD 1 JANUARY 2010 TO 31 MARCH 2010**

**BY: CHIEF FINANCIAL OFFICER**

**1. REASON FOR REPORT**

- 1.1 To advise Committee on matters relating to the Treasury Management function for the fourth 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.**

**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 fourth quarter of 2009/10 saw activity indicators suggest that a double-dip recession has been avoided and the Chancellor revised down his forecast for public sector borrowing. Household spending was hit by the rise in VAT and the bad weather and CPI inflation increased to above 3%. The Monetary Policy Committee( MPC) paused Quantitative Easing and kept official interest rates on hold at 0.5%

**Economic Forecast**

- 3.4 The Council's Treasury Advisers, Sector, revised their interest rates forecast in February 2010 and their latest estimates are below.

	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13
Bank rate	0.50%	0.50%	0.50%	1.00%	1.50%	2.00%	2.50%	3.00%	3.25%	3.75%	4.25%	4.50%
5yr PWLB rate	3.10%	3.15%	3.20%	3.40%	3.65%	4.00%	4.30%	4.50%	4.65%	4.75%	4.80%	4.85%
10yr PWLB rate	4.35%	4.45%	4.50%	4.60%	4.70%	4.75%	4.90%	4.95%	5.10%	5.10%	5.15%	5.15%
25yr PWLB rate	4.75%	4.80%	4.85%	4.90%	5.00%	5.05%	5.10%	5.20%	5.30%	5.35%	5.35%	5.35%
50yr PWLB rate	4.75%	4.80%	4.85%	4.90%	5.05%	5.10%	5.15%	5.15%	5.30%	5.30%	5.30%	5.30%

- The forecast is based on moderate economic recovery and MPC inflation forecast being below target in two years' time.
- The first Bank Rate increase is expected to be in 2011; and to reach 4.5% by March 2013.
- Long term PWLB rates are expected to steadily increase to reach 5.30% by early 2013 due to huge gilt issuance, reversal of QE and investor concerns over inflation.
- There is considerable uncertainty in all forecasts due to the difficulties of forecasting the timing and amounts of Quantitative Easing reversal, the fiscal effect of a general election, speed of recovery of banks profitability and balance sheet position coinciding with changes in the consumer saving ratio.

### Long Term Borrowing

- 3.5 The total debt outstanding at 31 March 2010 was £128.0 million. The average length of debt was 39.5 years, and the average interest rate was 5.76%.
- 3.6 Capital expenditure forecasting identified a borrowing requirement prior to yearend. Therefore during the quarter, advantage was taken of favourable interest rates on 10 February 2010, to borrow £5 million from PWLB at 3.04% for 5 years.
- 3.7 The Council's debt outstanding at 31 March 2010 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: -

	£m	Average Rate (%)	Proportion of Total Debt (%)
PWLB	94.6	6.19	73.9

Market Loans	33.4	4.51	26.1
<b>TOTAL</b>	<b>128.0</b>	<b>5.76</b>	<b>100.0</b>

- 3.8 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 from Barclays Bank (£23.3 million) and EuroHypo Bank, Luxemburg (£10.1 million). A profile of long-term debt repayments for the current debt portfolio is shown as **APPENDIX 1**.

### **Short Term Borrowing**

- 3.9 During the quarter a total of £6.5 million at an average rate of 032% of temporary borrowing was undertaken and £5.8 million temporary loans were repaid. The value of temporary borrowing ranged between £7 million and £11.5 million. As at 31 March 2010 temporary borrowing of £10 million was held and from the following organisations.

<b>Organisation</b>	<b>Maturity Date</b>	<b>Borrowing Rate (%)</b>	<b>Amount £m</b>
London Borough of Greenwich	28 April 2010	0.28	2.0
London Borough of Greenwich	10 May 2010	0.30	3.0
Leicester City Council	3 August 2010	0.65	3.0
London Borough of Croydon	19 November 2010	0.60	2.0
			10.0

### **Investments**

- 3.10 During the period 1 January to 31 March 2010, surplus funds of between £670,000 and £16.3 million at any one time were deposited in Call Accounts with the Council's Bankers, Bank of Scotland and Alliance & Leicester at an average rate of 0.84%.
- 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 was 0.84% and the average LIBID rate was 0.40%.
- 3.12 As at 31 March 2010, £3.42 million was held on deposit in the Call Account with the Council's Bankers and £5 million with the Alliance & Leicester Call Account. The Council also has £2 million on deposit with the Icelandic bank, Landsbanki. That bank is in receivership and the deposit is currently frozen.
- 3.13 As previously reported, the Landsbanki Winding Up Board has accepted all Local authorities' claims as priority creditors subject to modifications around the penalty interest applicable to each claim. Objections to this decision have been filed by corporate bond holders and so a number of Authorities have been selected by the winding Up Board as "test cases" to argue the status of priority creditors in Icelandic Courts.
- 3.14 In order to expedite the earliest possible resolution, our legal advisers Bevan Brittan have referred all local authority claims to court now to await the outcome of the "test cases". Evidence files have been deposited with our legal advisers but the court process in Iceland is likely to take 12 months.
- 3.15 Offers to buy Icelandic Bank bankruptcy claims are being made by a number of different companies and the range of offers vary significantly. It is not unusual in insolvency processes such as this for financial institutions to seek to purchase other organisations debts. To date no UK local authority has accepted one these offers.
- 3.15.1 The Council has been approached by an organisation which has expressed an interest in purchasing the Council's Landsbanki claim. They have indicated that they would pay between 40-45 pence in the pound for the claim. Current indications are that with priority status, the Council will receive 89p in the pound or 32p if priority status is overturned by the legal challenge. There is no certainty that the organisation would actually be prepared to pay the amount indicated. No further action is proposed regarding this approach at this time.

### **Counterparty List**

3.16 The Chief Financial Officer maintains a Counterparty list which is reviewed daily and complies with the criteria detailed in para 3.17.1. The criteria are regularly reviewed and any revision is submitted to Committee for approval as necessary.

3.17 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.

3.17.1 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)

3.18 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.

3.18 The Counterparty List has been amended to reflect a reduction in the maximum lending period to Barclays Bank from 364 days to six months arising from movement in the credit worthiness matrix (**APPENDIX 3**).

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

3.19 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.

3.20 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 is shown below.

### Treasury Prudential Indicators

	<b>Estimate 2009/10</b>	<b>Actual 2009/10 at 31 March 2010</b>
	<b>£ m</b>	<b>£ m</b>
<b>Authorised Limit for Authorised Debt</b>	174,147	174,147
<b>Operational Boundary for External Debt</b>	169,147	138,017
<b>Upper Limit on Fixed Interest Exposure</b>	100%	75.80%
<b>Upper Limit on Variable Interest Exposure</b>	30%	24.20%

<b>Maturity Structure</b>	<b>Lower</b>	<b>Upper</b>	<b>Actual to 31 March 2010</b>
Under 12 months	0%	15%	0.36%
1 – 2 years	0%	50%	0.36%
2 – 5 years	0%	50%	1.09%
5 – 10 years	0%	75%	1.63%
10 years & above	0%	100%	96.56%

## **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.**