

REPORT TO: POLICY AND RESOURCES COMMITTEE ON 25 MAY 2010

SUBJECT: ANNUAL TREASURY MANAGEMENT PERFORMANCE - 2009/10

BY: CHIEF FINANCIAL OFFICER

1. REASON FOR REPORT

- 1.1 To provide Committee with the Treasury Management annual report for the year ended 31st March 2010.
- 1.2 This report is submitted to Committee in terms of Section A (3) Council's Administration 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 The Chartered Institute of Public Finance and Accountancy updated its Code of Practice on Treasury Management in 2009. All Treasury Management activities are carried out in accordance with the Code.

The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy, which sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices, which set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the Council of an annual treasury management strategy report for the year ahead and an annual review report of the previous year.
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions to the Chief Financial Officer.
- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to Policy and Resources Committee.

Treasury management in this context is defined as:

“The management of the local authority’s cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks. ”

4. TREASURY PERFORMANCE

4.1 This annual Treasury Management performance report covers

- ❖ the economy and interest rates in 2009/10;
- ❖ investment outturn for 2009/10;
- ❖ the Council’s long term borrowing as at 31 March 2010;
- ❖ long term borrowing and debt repayment
- ❖ short term borrowing

4.2 The Economy and Interest Rates

4.2.1 During 2009/10 the Bank of England Monetary Policy Committee (MPC) was focused on helping the economy face the longest recession the UK had experienced for many years. Despite keeping the Bank Rate at an unprecedented historical low of 0.5% throughout the year, the MPC also had to resort to extreme measures in terms of introducing liquidity into the economy through quantitative easing by purchasing £200 billion of gilts and corporate bonds. This had the effect of boosting prices for gilts and corporate bonds and therefore bringing down yields. The impact of which, was to reduce borrowing costs for both the corporate and public sector.

4.2.2 The increase in money supply in the economy generated by the quantitative easing programme brought the credit crunch induced spread between Bank Rate and 3 month LIBID (investment rate that depositors could earn) down from 0.95% at the beginning of the financial year to zero during August 2009.

- 4.2.3 The dominant focus of the economy in 2009/10 was on quarterly GDP growth figures. In technical terms, the recession bottomed out in quarter 1 of 2009. There was then major disappointment that the end of the recession failed to materialise in quarter 3 2009 but the fourth quarter of 2009 did then see economic growth return at +0.4%.
- 4.2.4 Inflation has not been a major concern for the MPC as it fell back below the 2% (CPI) target level from June to November. However, it did spike upwards to reach 3.5% on the back of the end of the temporary cut in VAT on 1 January 2010. This was not seen as a cause for alarm as this spike was expected to fall out of the inflation index and inflation was forecast by the Bank of England to fall back under target by the end of 2010.

4.3 2009/10 Treasury Management Strategy

- 4.3.1 The Councils Treasury Management Strategy was approved by the Council at its meeting on 12 February 2009 (Para 6 refers).
- 4.3.2 The major issue for treasury management in 2009/10 has been the huge difference between investment rates and borrowing rates that has emerged during the recession due to:-
- ❖ the unprecedented fall in Bank Rate
 - ❖ the disappearance during the year of the margins over more normal investment rates caused by the credit crunch as the Bank of England's quantitative easing operations had the desired effect
- 4.3.3 In order to balance the impact of the loss of investment income, there was re-evaluation of the benefits of new borrowing. Significant treasury management savings were achieved by reducing investment balances and borrowing for short periods instead of taking new borrowing to finance new capital expenditure. Whilst this has provided savings during 2009-10 in terms of debt management costs, the Chief Financial Officer is mindful of both interest rate risk and refinancing risk moving forward into 2010/11 in case interest rates begin to rise. This position is being actively monitored in association with the Council's Treasury Management Advisors.
- 4.3.4 The reduction of investment balances during the year has also meant a reduction in exposure to Counterparty and interest rate risk.
- 4.3.5 An option was taken to draw some shorter term (under 10 years) borrowing from PWLB during the year at lower interest rates. This assisted in lowering debt servicing costs in short-term whilst at the same time providing a degree of budget certainty for debt management. This reduced the risk of deferring the entire borrowing requirement until later years when interest rates could be higher.

4.3.6 The Council operated both short-term borrowing and investment portfolios during the year and as a consequence was at lower risk from being exposed to the impact of a sharp, unexpected rise in short-term variable interest rates.

4.4 Investment Outturn for 2009/10

4.4.1 The Council manages its investments in-house and invests with the institutions listed on the Council's approved Counterparty list.

4.4.2 In addition to credit agency ratings, the Council's Treasury Management Advisors provide a creditworthiness matrix to aid the assessment of risk involved in lending to individual counterparties. The Council's Counterparty List is continually monitored in conjunction with this information.

4.4.3 The table below shows the overall investment undertaken by the Council during 2009/10.

	Total Sum Deposited (£)	Average Rate (%)
Approved Financial Institutions	31.86m	0.80
Council's Bankers	158.96m	0.85
TOTAL	190.82m	0.84

The above figures are cumulative and the actual amounts invested at any one time ranged from £30,000 to £16.3 million

4.4.4 Performance of investments is benchmarked against the average 7 day London Interbank Bid Rate (LIBID). During the year the average achieved was 0.84% and the LIBID average rate was 0.42%.

4.4.5 The Council currently has £2 million frozen in the Icelandic bank, Landsbanki. The Local Government Association is coordinating the efforts of all UK authorities with Icelandic investments. Members have been periodically updated on the latest developments on these efforts and the latest position was reported to Policy and Resources Committee on 27 April 2010.

The Scottish Parliament has issued regulations to allow local authorities to delay recognising any loss on these investments that may eventually be incurred until the financial year 2010-11.

4.5 Long Term Borrowing and Debt Repayment

4.5.1 The Council's long term external debt position at 31 March 2010 compared with the position at the end of last financial year was as follows:

	31 March 2009			31 March 2010		
	Actual (£000)	Rate (%)	Average Life (Years)	Actual (£000)	Rate (%)	Average Life (Years)
Fixed Rate Funding						
PWLB	104,771	6.07	34.26	94,617	6.19	30.90
Market	-	-	-	-	-	-
Variable Rate Funding						
PWLB	-	-	-	-	-	-
Market	33,400	4.51	64.83	33,400	4.51	63.83
Total Debt	138,171	5.69		128,017	5.75	

4.5.2 Capital expenditure forecasting during the year identified a borrowing requirement of £9 million, therefore advantage was taken of favourable rates in February 2010 to borrow £5 million from PWLB at 3.04%.

4.5.3 It was decided to use investment balances to repay longer term debt when a peak in PWLB rates occurred. Advantage was taken of two of these peaks.

- ❖ In April 2009 £12.9million of 43 year PWLB debt at 4.35% compared to the rate then available on investing of 0.85%. This enabled the Council to make a saving of £505,552 per annum on interest payments.
- ❖ In May 2009 £2 million of 43 year PWLB debt at 4.35% was repaid. This enabled the Council to make a saving of £80,000 per annum on interest payments.

These repayments helped to smooth the Council's repayment profile and also reduced counterparty risk by reducing investment balances.

4.6 Short Term Borrowing during 2009/10

4.6.1 During the quarter a total of £6.5 million at an average rate of 0.32% 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.

4.6.2 As at 31 March 2010 temporary borrowing of £10 million was held and from the following organisations.

Organisation	Maturity Date	Borrowing Rate (%)	Amount £m
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

5. 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 maintaining a sound long term debt portfolio, while retaining flexibility to take advantage of any opportunities which were afforded.

(d) Consultations

None.

6. CONCLUSION

6.1 The Council's requirement for funds continues to be managed in accordance with the agreed strategy

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Background Papers: Papers held in Payments Section
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