

**AGENDA ITEM:** Pages 87 – 94

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Meeting	Cabinet Resources Committee
Date	2 September 2010
<b>Subject</b>	<b>Treasury Management Outturn for the quarter ended 30 June 2010</b>
Report of	Cabinet Member for Resources and Performance
Summary	To report on Treasury Management activity in the quarter to 30 June 2010

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Officer Contributors	Chris Malyon – Assistant Director of Finance Karen Bannister – Interim Treasury Manager
Status (public or exempt)	Public
Wards affected	Not applicable
Enclosures	Appendix – Deposits as at 30 June 2010 with Credit Ratings
For decision by	Cabinet Resources Committee
Function of	Executive
Reason for urgency / exemption from call-in (if appropriate)	Not applicable

Contact for further information: Karen Bannister, Interim Treasury Manager, 0208 359 7119.

## **1. RECOMMENDATIONS**

- 1.1 That the Treasury Management activity and outturn for the quarter ended 30 June 2010 be noted.**
- 1.2 That the Committee consider any areas on which it would like to receive further information.**

## **2. RELEVANT PREVIOUS DECISIONS**

- 2.1 Cabinet Resources Committee, 25 March 2008 (Decision item 18) – Treasury Management Business Strategy.
- 2.2 Cabinet, 23 October 2008 (Decision item 12) – Council Deposits in Icelandic Banks.
- 2.3 The Leader of the Council and Cabinet Member for Resources approved under delegated powers (DPR 712) on 5 December 2008 the Treasury Management Strategy 2008/09 – Deposit Counterparty Limits.
- 2.4 Cabinet Resources Committee, 19 January 2009 (Decision item 16) – Treasury Management Strategy.
- 2.5 Cabinet Resources Committee, 30 March 2009 (Decision item 13) – Treasury Management Strategy.
- 2.6 Cabinet Resources Committee, 15 June 2009 (Decision item 7) – Outturn 2008/09.
- 2.7 Cabinet Resources Committee, 2 September 2009 (Decision item 15) – Treasury Management Activity in the Quarter to 30 June 2009.
- 2.8 Cabinet Resources Committee, 2 November 2009 (Decision item 14) – Treasury Management Activity to 31 August 2009.
- 2.9 Cabinet Resources Committee, 19 January 2010 (Decision item 9) – Treasury Management Activity to 18 December 2009.
- 2.10 Cabinet Resources Committee, 23 February 2010 (Decision item 10) – Treasury Management Activity to 31 December 2009.
- 2.11 Cabinet Resources Committee, 16 March 2010 (Decision item 9) – Treasury Management Strategy 2010/11.
- 2.12 Special Committee (Constitution Review), 25 March 2010 (Decision item 8) – Amending the Council’s Financial Regulations.

## **3. CORPORATE PRIORITIES AND POLICY CONSIDERATIONS**

- 3.1 The Treasury Management Strategy (TMS) ensures effective treasury management supports the achievement of the Council’s corporate priority for 2010-2013, ‘Better services with less money’, through the strategic objective “make sure we get best value from resources across the public sector, including our people and assets”. The TMS is committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

#### **4. RISK MANAGEMENT ISSUES**

- 4.1 Borrowing and deposit rates are determined by the market and can be volatile at times. Officers mitigate this volatility by monitoring the interest rate market in conjunction with treasury advisors and brokers, and by actively managing the debt and deposit portfolios.
- 4.2 There is a risk of the Council becoming too risk averse in its response to this situation, and not achieving budgeted deposit income.
- 4.3 The United Kingdom's AAA Sovereign rating is at risk of being downgraded. The impact of such a downgrade will be addressed when in the future Treasury Management Strategy updates to be approved by the Cabinet Resources Committee.

#### **5. EQUALITIES AND DIVERSITY ISSUES**

- 5.1 The management of the Council's cash flow ensures the availability of adequate monies to pay for the delivery of the authority's public duties.

#### **6. USE OF RESOURCES IMPLICATIONS (Finance, Procurement, Performance and Value for Money, Staffing, IT, Property, Sustainability)**

- 6.1 During the 2009/2010 financial year the Council achieved £1.65m of net interest benefit.
- 6.2 The wider financial implications for the Council are dealt with in section 9 of this report.

#### **7. LEGAL ISSUES**

- 7.1 None other than those mentioned in the body of this report.

#### **8. CONSTITUTIONAL POWERS**

- 8.1 Financial Regulations (Part 1, Section 7) within the Council Constitution state:
  - (1) This organisation adopts the key recommendations of CIPFA's Treasury Management in the Public Services Code of Practice (the Code), as described in Section 4 of that code.
  - (2) Cabinet Resources Committee will create and maintain a Treasury Management Policy Statement, stating the policies and objectives of its treasury management activities.
  - (3) The Chief Finance Officer will create and maintain suitable Treasury Management Practices (TMPs).
  - (4) The content of the policy statement and TMPs will predominantly follow the recommendations contained in Section 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the organisation. Such amendments will not result in the authority materially deviating from the Code's key recommendations.
  - (5) Cabinet Resources Committee will receive reports on its treasury management policies, practices and activities, including an annual strategy and plan in advance of the year, and an annual report after its close in the form prescribed in the TMPs. These reports will incorporate the prudential borrowing limits and performance indicators.

## **9. BACKGROUND INFORMATION**

### **9.1 Treasury Management Strategy 2009/10**

- 9.1.1 The Council's Treasury Management Strategy 2010/11 was approved at Cabinet Resources Committee on 16 March 2010. The TMS 2010/11 is a continuation of the 2009/10 strategy pending the tender and appointment of Treasury Advisors. The TMS 2010/11 reflects the Council Budget 2010-2011 Forward Plan and Capital Programme. They set out the timeframes and credit criteria for placing cash deposits and the parameters for undertaking any further borrowing.
- 9.1.2 The key changes were:
- (i) The introduction of liquidity and security benchmarks, as required by CIPFA Treasury Management Code of Practice, are outlined in Annex A to the Treasury Management Strategy;
  - (ii) The removal of references to Money Market Funds; and
  - (iii) The reference to the use of a minimum sovereign rating now applies only to non-UK institutions. This reflects the risk that the UK sovereign rating may be downgraded.
- 9.1.3 Following the banking crisis in 2008, a number of amendments were made to counter party criteria, initially by Cabinet in October 2008 and then subsequently under delegated powers by the Leader (who at that time was also the Cabinet Member for Resources). The amendments sought to reduce risk by raising the bar on minimum counterparty ratings as the uncertainty over the financial stability of financial institutions grew.
- 9.1.4 The TMS is under constant review to reflect market conditions and the financing requirements of the Council.
- 9.1.5 In the quarter ended 30 June 2010, the Council placed 145 deposits with a total value of £1,240m and had 134 deposits worth £1,194.5m repaid.

### **9.2 Icelandic Bank Deposits**

- 9.2.1 The Icelandic Government has stated its intention to honour all its commitments as a result of their banks being placed into receivership. The U.K. Government is working with the Icelandic Government to help bring this about. At the current time, the process of recovering assets is still ongoing with the Administrators. The Local Government Association is coordinating the efforts of all UK authorities with Icelandic deposits. Members will be periodically updated on the latest developments on these efforts.
- 9.2.2 On 9 December 2009, Bevan Brittan, the solicitors acting on behalf of the LGA, received notification from the Glitnir Winding-up Board that they had accepted all local authority claims as general unsecured claims, rather than priority claims.
- 9.2.3 Bevan Brittan actively challenged this decision prior to the Creditor's meeting on 17 December 2009, but, it was not possible to reach an agreement. A mediation process has taken place and there has been no change to the general unsecured position. Therefore, it is now a matter for the Icelandic judicial system.
- 9.2.4 Without priority status local authorities are likely to get in the region of 25-30 per cent of their deposits back rather than 95% to 100% as previously assumed.
- 9.2.5 The 2009/10 accounts, which assume local authorities have priority status, include impairments adjustments to the General Fund as prescribed by Financial Reporting Standards and LAPP updates. The risk is managed through the Risk Reserve.

### 9.3 Economic background for the Quarter Ended 30 June 2010

- 9.3.1 The UK economy continues to emerge from the effects of the financial crisis. Whilst the recovery is likely to gather pace over the next year, the effects of the crisis are likely to persist resulting in further financial market volatility.
- 9.3.2 At the June meeting, The Bank of England's Monetary Policy Committee voted to maintain the official Bank Rate at 0.5% and to maintain the £200bn stock of gilts and corporate bonds. It is expected that the official Bank Rate will hold steady for the remainder of the year.
- 9.3.3 The spread between Bank Rate and 3 month LIBID (investment rate that depositors could earn) increased slightly during the quarter from zero to 0.07% at 30 June 2010.
- 9.3.4 Gross Domestic Product (GDP) increased by 1.1% in the second quarter of 2010, compared with an increase of 0.3% in quarter one. The growth was spread broadly across services, construction and production.
- 9.3.5 CPI inflation remained above the 2% target at 3.2%, due to the restoration of the standard rate of VAT to 17.5%, higher oil prices and the past depreciation of sterling. These temporary effects on inflation are expected to wane resulting in downward pressure that is likely to cause inflation to fall below the 2% target. However, the pace and extent of moderation in inflation are highly uncertain.
- 9.3.6 The long-term interest rate (Public Works Loan Board (PWLB) 50 year maturity) started the quarter at 4.70% and then fell to 4.32% at 30 June 2010.
- 9.3.7 The TMS will be kept under review specifically in terms of market conditions, benchmarks and yield.

### 9.4 Borrowing Performance

- 9.4.1 A borrowing requirement of £56.32m (£10.5m is Housing Revenue Account) is currently forecast for 2010/11. The capital program is kept under constant review and any changes that impact on the external borrowing will be reported to the Cabinet Resources Committee.
- 9.4.2 The total value of long term loans dropped from £214.5m at 31 March 2010 to £207.5 at 30 June 2010. Had borrowing been necessary it may have resulted in an increase in the average borrowing rate.

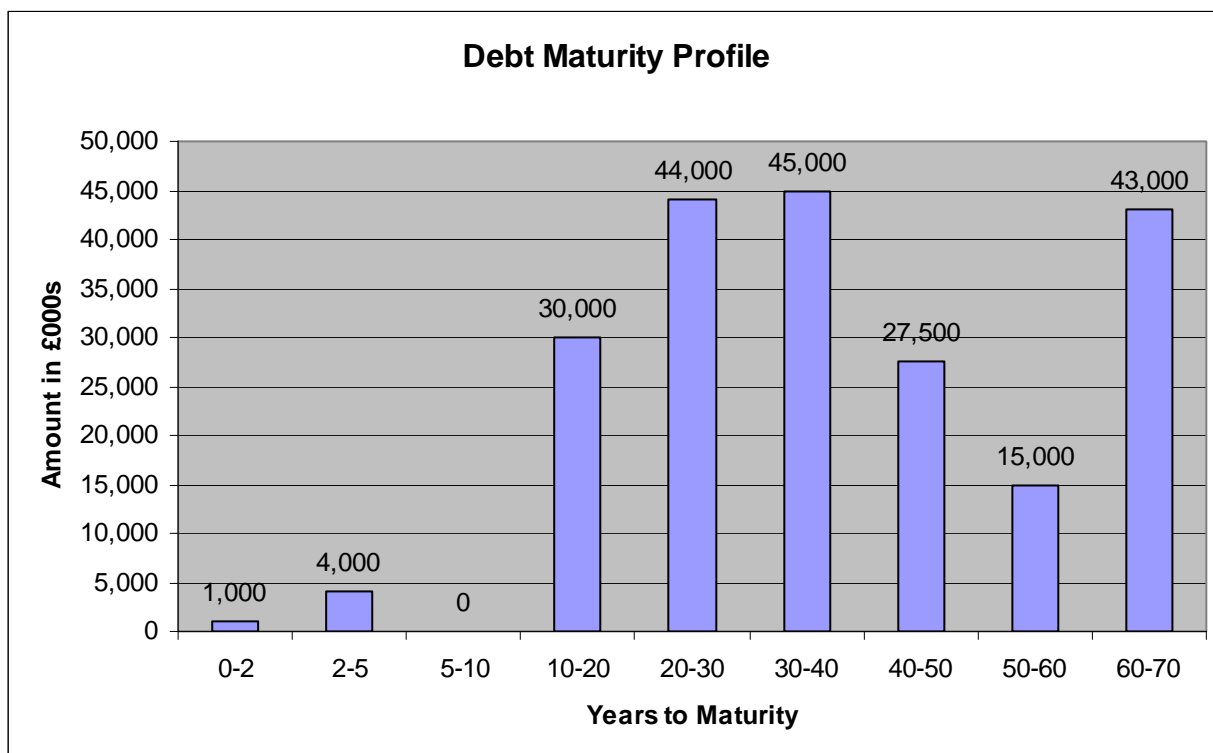
### 9.5 Current Portfolio

- 9.5.1 The Council's long term debt position at the beginning and end of the half year was as follows:

	30 June 2010		31 March 2010	
	Principal	Average Rate	Principal	Average Rate
PWLB	£140.00m	4.19%	£147.00m	4.21%
Market	£62.50m	3.82%	£62.50m	3.82%
Temporary	£5.00m	4.50%	£5.00m	4.50%
	£207.50m	4.09%	£214.50m	4.09%

- 9.5.2 The Council's long term debt portfolio is a mixture of PWLB and market loans in the form of LOBOs (Lender's Option Borrower's Option), loans that are at a fixed interest rate for an initial period, following which the lender can change the interest rate but the borrower has the option to repay the loan if the rate is changed and not considered value for money.

The Council's current debt maturity profile is outlined in the graph below.



- 9.5.3 As the cost of borrowing is expected to rise and the Council's average rate of borrowing is relatively low at 4.09%, a decision was made not to proceed with any early debt redemption. However, this will be reviewed on a quarterly basis as part of the treasury management review.
- 9.5.4 In order to comply with accounting standards for financial instruments, some of the market loans in the debt portfolio have been recalculated on an effective interest rate basis as apposed to being calculated on an amortised cost basis. The total value of loans in question before re-measurement was £9.5m; and additional charge of 0.36m has now been added to the carrying value of these loans.

## 9.6 Investment Performance

- 9.6.1 Deposits are managed internally. At the 30<sup>th</sup> of June 2010 deposits outstanding amounted to £247.450m (£82.13m of which is Pension Fund Cash), achieving an average rate of return of 0.404% (adjusted for Icelandic deposits) against a benchmark of 0.2%.
- 9.6.2 The benchmark is the average 7-day LIBID rate (un-compounded), sourced from the Financial Times. The LIBID rate or London Interbank Bid Rate is the rate that a Euromarket bank is willing to pay to attract a deposit from another Euromarket bank in London.
- 9.6.3 The Council outperformed the benchmark return in the quarter by 0.204%, which based on the average balance invested for the year produced some £504,700 additional interest.

## 9.7 Prudential Indicators

- 9.7.1 The prudential indicators will be reviewed and reported to this committee before the end of September as part of the revised Treasury Management Strategy.

## **9.8 Compliance**

- 9.8.1 The current TMS was approved by this Committee on 17 March 2010. The TMS demands regular compliance reporting to this Committee to include an analysis of deposits made during the review period. This also reflects good practice and will serve to reassure this committee that all current deposits for investment are in line with agreed principles as contained within the corporate TMS.
- 9.8.2 As at 30 June 2010, the Council had deposits outstanding with a total value of £247.45m (£82.13m of which is Pension Fund cash) of which four Icelandic deposits totalling £27.4m fell outside the TMS as approved on 17 March 2010. A list of deposits outstanding and counterparty credit ratings at 30 June 2010 is attached in the appendix to this report.
- 9.8.3 All Deposits placed during the quarter ended 30 June 2010 were compliant with the TMS as approved on 17 March 2010.
- 9.8.4 Treasury management procedures are monitored and reviewed in light of new CIFPA guidance and current market conditions.

## **10. LIST OF BACKGROUND PAPERS**

- 10.1 None.

Legal – JO'H  
CFO – CM/AT

DEPOSITS AS AT 30 JUNE 2010

Category	Deal Number	Counter Party	Deposit Date	Maturity Date	Rate of Interest	Amount Outstanding	Fitch Rating			Moody's Rating			S&P Ratings				
							S Term	L Term	Indiv	Support	S Term	L Term	Fin Stgth	S Term	L Term		
							<b>Government Backed</b>										
							<b>Local Authorities</b>										
1	2000010676	DEBT MANAGEMENT OFFICE	02-Jun-10	01-Jul-10	0.25	20,000,000											
1	2000010700	DEBT MANAGEMENT OFFICE	17-Jun-10	02-Aug-10	0.25	6,000,000											
1	2000010725	DEBT MANAGEMENT OFFICE	30-Jun-10	01-Jul-10	0.25	2,200,000											
2	2000010722	BLACKPOOL BOROUGH COUNCIL	30-Jun-10	01-Jul-10	0.32	6,000,000											
2	2000010674	DOVER DISTRICT COUNCIL	01-Jun-10	01-Jul-10	0.3	10,000,000											
2	2000010688	DUMFRIES & GALLOWAY COUNCIL	10-Jun-10	10-Sep-10	0.3	3,000,000											
2	2000010636	EAST DUNBARTONSHIRE CNCL	10-May-10	10-Aug-10	0.45	1,500,000											
2	2000010655	EAST DUNBARTONSHIRE CNCL	26-May-10	26-Aug-10	0.4	5,000,000											
2	2000010602	EASTLEIGH B C	16-Apr-10	16-Jul-10	0.4	5,000,000											
2	2000010647	EASTLEIGH B C	18-May-10	30-Jul-10	0.3	5,000,000											
2	2000010649	EXETER CITY COUNCIL	21-May-10	30-Jul-10	0.3	5,000,000											
2	2000010666	KIRKLEES COUNCIL	28-May-10	01-Jul-10	0.35	1,500,000											
2	2000010670	KIRKLEES COUNCIL	01-Jun-10	02-Aug-10	0.35	3,500,000											
2	2000010724	LONDON BOROUGH OF CAMDEN	30-Jun-10	01-Jul-10	0.3	6,650,000											
2	2000010693	LONDON BOROUGH OF MERTON	11-Jun-10	10-Sep-10	0.3	1,000,000											
2	2000010712	MID SUFFOLK DISTRICT CNCL	22-Jun-10	14-Jul-10	0.3	1,500,000											
2	2000010650	PLYMOUTH CITY COUNCIL	24-May-10	30-Jul-10	0.3	3,000,000											
2	2000010681	PLYMOUTH CITY COUNCIL	09-Jun-10	01-Jul-10	0.28	3,000,000											
2	2000010713	REDDITCH BOROUGH COUNCIL	22-Jun-10	21-Sep-10	0.3	1,500,000											
2	2000010723	REDDITCH BOROUGH COUNCIL	30-Jun-10	02-Aug-10	0.3	2,000,000											
2	2000010678	SALFORD CITY COUNCIL	02-Jun-10	31-Aug-10	0.3	2,800,000											
2	2000010690	SHEFFIELD CITY COUNCIL	10-Jun-10	10-Sep-10	0.3	5,000,000											
2	2000010692	SHEFFIELD CITY COUNCIL	11-Jun-10	10-Sep-10	0.3	5,000,000											
2	2000010707	SHEFFIELD CITY COUNCIL	21-Jun-10	02-Aug-10	0.3	3,000,000											
2	2000010708	SHEFFIELD CITY COUNCIL	21-Jun-10	31-Aug-10	0.3	2,000,000											
2	2000010703	SOUTHAMPTON CITY COUNCIL	18-Jun-10	29-Jul-10	0.29	4,000,000											
2	2000010616	SOUTHEND-ON-SEA BC	26-Apr-10	05-Jul-10	0.45	5,000,000											
2	2000010622	SOUTHEND-ON-SEA BC	30-Apr-10	05-Jul-10	0.45	5,000,000											
2	2000010656	SWINDON BOROUGH COUNCIL	20-May-10	30-Jul-10	0.3	5,000,000											
2	2000010697	SWINDON BOROUGH COUNCIL	16-Jun-10	02-Jul-10	0.3	5,000,000											
2	2000010706	WEST YORKSHIRE F & R AUTH	21-Jun-10	22-Jul-10	0.3	1,600,000											
4	2000005708	ROYAL BANK OF SCOTLAND	17-Jun-10	17-Sep-10	0.61	5,000,000	F1+	A-	F	1	P-1	A3	E	A-1	A-		
4	2000010673	ROYAL BANK OF SCOTLAND	01-Jun-10	01-Jul-10	0.43	20,000,000	F1+	AA-	D/E	1	P-1	Aa3	C-	A-1	A+		
4	2000010341	BANK OF SCOTLAND CORPORAT	09-Sep-09	call account	0.75	25,000,000	F1+	AA-	C	1	P-1	Aa3	D+	A-1	A+		
5	2000010527	BARCLAYS COMMERCIAL BANK	11-Feb-10	call account	0.4	25,000,000	F1+	AA-	B	1	P-1	Aa3	C	A-1+	AA-		
5	2000010643	BARCLAYS COMMERCIAL BANK	14-May-10	13-Aug-10	0.68	9,300,000	F1+	AA-	B	1	P-1	Aa3	C	A-1+	AA-		
		<b>Building Societies</b>					<b>&gt;£50billion up to 182 days or £25billion to £50 billion up to 90 days</b>										
		None															
		<b>Investments outside TMS</b>															
		<b>Icelandic Banks</b>															
	2000005163	GLITNER BANK (ICELAND)	07-Nov-06	frozen	5.62	7,000,000											
	2000005218	GLITNER BANK (ICELAND)	24-Jan-07	frozen	6.11	3,000,000											
	2000005226	GLITNER BANK (ICELAND)	07-Feb-07	frozen	6.13	2,400,000											
	2000005511	LANDISBANKI ISLANDS H.F.	28-Sep-07	frozen	6.47	15,000,000											
		<b>TOTAL VALUE OF INVESTMENTS LESS ICELANDICS</b>				<b>247,450,000</b>											
		<b>TOTAL VALUE OF INVESTMENTS OUTSIDE TMS LESS ICELANDICS</b>				<b>220,050,000</b>											
		<b>TOTAL VALUE OF INVESTMENTS OUTSIDE TMS LESS ICELANDICS</b>				<b>27,400,000</b>									<b>0</b>		

Comments on Redemption (if known)