

<b>REPORT TO</b>	<b>DATE OF MEETING</b>
Cabinet	16 November 2011



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<b>SUBJECT</b>	<b>PORTFOLIO</b>	<b>AUTHOR</b>	<b>ITEM</b>
Treasury Management Activity Mid year review	Finance & Resources	G Whitehead	4

## 1 Summary and link to corporate objectives

This report includes investment activity to 13 September 2011. It advises that, on average, the Council had surplus cash balances of £12.1m on which it received a return of 1.02% during the first five months of 2011/12.

In response to the turbulence in the financial markets the Council's Treasury Advisor, Sector, has recommended restricting deposit periods to three months, for all institutions excepting the part nationalised banks.

It confirms compliance with the prudential indicators specified in the Treasury Strategy.

The report will also be considered by Council, at its meeting on 23 November 2011.

## 2 Recommendations

Cabinet is asked

- To note the report and
- Approve the limit of three months on term deposits with institutions other than the nationalised banks.

## 3 Details and reasoning

The Code of Practice for Treasury Management specifies that Councils should review their treasury strategy and activity half yearly. This report meets that requirement.

## 4 Interest rate forecast

The following table shows the interest rate forecast of the Council's Treasury Advisor, Sector Treasury Services Ltd.

	Now %	Dec 2011 %	Mar 2012 %	June 2012 %	Sep 2012 %	Mar 2013 %	June 2013 %	Dec 2013 %	Mar 2014 %
Base rate	0.50	0.50	0.50	0.50	0.75	1.25	1.50	2.50	3.00
5 yr PWLB	2.45	2.70	2.90	3.00	3.10	3.40	3.60	4.00	4.10
10 yr PWLB	3.75	4.00	4.10	4.30	4.40	4.60	4.70	4.90	5.00
25 yr PWLB	4.90	5.00	5.10	5.10	5.10	5.20	5.30	5.40	5.50
50 yr PWLB	4.95	5.00	5.10	5.10	5.10	5.20	5.30	5.40	5.50

Comparison with the forecast of six months ago, when the Treasury Strategy was drafted, shows that the timing of the first assumed increase in base rate has slipped by nine months. It also shows that current PWLB 5 and 10 years rates are 0.75% lower than they were then. All of these factors reflect the concerns about the economy at home and abroad.

## 7 Review of the Treasury Strategy:

The Treasury Management and Investment Strategies for 2010/11 were approved by Council on 2 March 2011. They defined the Council's investment priorities as the security of capital sums invested and the maintenance of liquidity. Consistent with these priorities it would also seek to achieve the optimum return (yield) on investments.

The strategies fixed limits on the amounts that could be invested with individual institutions, and the length of investment, based on each institution's credit ratings, credit alerts, and credit default spreads. These limits are detailed in appendix B.

Consideration has been given, in light of the turbulence, uncertainty and fear in financial markets, as to whether any changes in the list or the limits are required, and the advice of our Treasury Advisors has been sought. They have replied that:

"Sector sees no imminent concerns with any of the institutions, durations and limits that you have set out. Sector would suggest keeping investments short dated (no longer than 3 months), but with regard to the rates offered by Bank of Scotland and Lloyds for longer periods (up to 12 months) would make an exception as the likelihood of these institutions coming under any significant threat is highly unlikely due to the fact that they are part nationalised.

In the current economic climate Sector suggests placing investments with Money Market Funds --- since they offer diversification amongst a range of different asset classes and counterparties"

The implications of this guidance is that Santander and Nationwide, which would have a time limit of 6 months based on the normal credit assessment, have been reduced to a three months. The Council's own bank HSBC, which would be twelve months, also falls to three months. Barclays time limit based on the normal credit assessment is only three months, so no reduction is necessary.

There is one existing investment that falls marginally outside this new limit. A £1m deposit with Nationwide will mature on January 3rd 2012

## 8 Treasury activity

Investment activity in the half year is summarised in the following table:

	Average Daily investment. £'000	Earnings to 13/9/2011 £	Average Rate %
DMO	9	10	0.25
Other fixed term deposits	5,066	35,186	1.53
Call accounts	6,993	20,852	0.66
Council's own bank	65	0	0
	<u>12,133</u>	<u>56,047</u>	<u>1.02</u>

The above table excludes the Icelandic loans. These are commented on below.

A full list of investments currently held is shown at Appendix A.

The interest earning benchmark is the average LIBID 7 day rate. This was 0.47% as at 13/9/2011. The authority has outperformed the benchmark.

The following table compares the budgets for interest receivable against the latest projection. It will be seen that very little difference is predicted.

	Budget for year £'000	Actual to 13/9/2011 £'000	Forecast for year £'000
Interest earned			
On current investments	(95)	(56)	(103)
On Icelandic loans	(175)	(81)	(177)
Net cost/(surplus)	(270)	(137)	(280)

## 9 Icelandic Loans

There have been two further repayments made by the Administrator of the Heritable Bank (19 April and 15 July) totalling 10.3% or £208k. The total repaid is now 60.4% or £1.217m. The Administrator's latest advice is of a likely repayment between 86% and 90%, with a "stressed" return of between 74% and 80%. The accounts at March 2011 assumed a recovery of 85%.

In respect of Landsbanki deposits, the Icelandic Supreme Court hearing that will decide whether Council's retain their priority status, is due to be held on September 14 and 15, with a decision to be announced within the following month.

## 10 Borrowing:

The Treasury Strategy indicated that no borrowing was necessary over the next 2 to 3 years. This remains the case and no borrowing is planned.

## 11 Prudential Indicators:

It is a statutory duty for the Council to determine and keep under review the "Affordable Borrowing Limits" which were reported in the approved Treasury Management Statement.

The following table shows the approved limits and the current position:

Prudential Indicator	March 2011 Indicator £'000	Actual £'000
Capital Financing Requirement (CFR) March 2011	6,154	5,917
Gross borrowing	0	0
Investments (note 1) actual as at 22/8/11	(5,506)	(14,300)
Net borrowing/(investments) actual at 22/8/11	(5,506)	(14,300)
Authorised limit for external debt (note 2)	6,154	1,708
Operational boundary for external debt (note 2)	1,800	1,708
Limit of fixed interest rates (based on net debt)	2,250	1,708
Limit of variable interest rates (based on net debt)	100% on inv cash	100%
Principal sums invested for periods exceeding 364 days	0	0
Maturity structure of borrowing limits		
Under 12 months	N/A	N/A
12 months to 2 years	N/A	N/A
2 years to 5 years	N/A	N/A
5 years to 10 years	N/A	N/A
10 years and above	N/A	N/A

Note 1 - The prudential indicators assumed investments, excluding outstanding Icelandic loans, of £5.506m at March 2011 falling to £5.066m at March 2012. The actual value at March 2011 was £7.2m and is currently £14.3m. This is expected to fall significantly by year end.

Note 2 – The figure of £1.708m is not borrowings, but amounts owing under finance lease arrangements. The actual shown is as at March 2011

## 12 WIDER IMPLICATIONS

In the preparation of this report, consideration has been given to the impact of its proposals in all the areas listed below, and the table shows any implications in respect of each of these. The risk assessment which has been carried out forms part of the background papers to the report.

<b>FINANCIAL</b>	The financial implications are outlined within the report.		
<b>LEGAL</b>	Compliance with various Regulations and statutory Codes of Practice		
<b>RISK</b>	The Council's treasury management strategy and policies are designed to ensure the effective control and management of the risks associated with such activities.		
<b>OTHER (see below)</b>			
<i>Asset Management</i>	<i>Corporate Plans and Policies</i>	<i>Crime and Disorder</i>	<i>Efficiency Savings/Value for Money</i>
<i>Equality, Diversity and Community Cohesion</i>	<i>Freedom of Information/ Data Protection</i>	<i>Health and Safety</i>	<i>Health Inequalities</i>
<i>Human Rights Act 1998</i>	<i>Implementing Electronic Government</i>	<i>Staffing, Training and Development</i>	<i>Sustainability</i>

## BACKGROUND DOCUMENTS

Financial Strategy/Budget and Council Tax 2011/12  
 Treasury Management in the Public Services: Code of Practice  
 CIPFA Prudential Code for Capital Finance in Local Authorities

## Appendix A

### Investments as at 13 September 2011

<b>Counterparty</b>	<b>Type</b>	<b>Amount £'000</b>	<b>Rate %</b>	<b>Date of investment</b>	<b>Maturity</b>
Santander	Term	1,000	1.13	28/06/11	28/09/11
Santander	Term	1,000	1.13	15/07/11	17/10/11
Lancashire County Council	Term	1,000	1.46	08/11/10	08/11/11
Nationwide BS	Term	1,000	1.03	28/06/11	03/01/12
Lancashire County Council	Term	1,000	1.53	26/01/11	25/01/12
Bank of Scotland	Term	1,000	1.80	28/06/11	28/03/12
Bank of Scotland	Term	1,000	2.05	28/06/11	26/06/12
Bank of Scotland	Call	1,000	0.75		
Santander	Call	700	0.75		
Royal Bank of Scotland	Call	3,000	0.80		
Lancashire County Council	Call	1,000	0.70		
<b>Total</b>		<b>12,700</b>			

Outstanding Icelandic Loans have a book value of £3.042m at September 1 2011.

## Appendix B

### Current list of Financial Institutions and Investment Criteria

Investment Group	Category	Institutions	Sector Colour Code	Sovereign rating	Max period	Limit per Institution
Tier 1	Sovereign or Sovereign "type"	DMADF			6 months	No limit
		Local Authority			1 year	£3m
		UK Govt backed Money market funds			n/a instant access	£3m
Tier 2	UK Nationalised Institutions	None (N Rock deposits no longer guaranteed)				
Tier 3	Institutions guaranteed by other governments	None (Irish Banks removed from list)				
Tier 4A (nb 1 and 2)	UK Partly nationalised institutions; with access to funds under the Credit Guarantee Scheme	RBS group (inc Nat West)	Blue	AAA stable from all 3 agencies	12 months	£3m per group
		Lloyds Group (inc HBoS & Lloyds)	Blue		12 months	£3m per group
Tier 4B (nb 1 and 2)	Independent UK Institutions with access to the Credit Guarantee Scheme	HSBC	Orange	AAA stable from all 3 agencies	12 months	£2m
		Santander UK Nationwide	Red Red		6 months	£2m
		Barclays,	green		3 months	£2m
Tier 5	Money Market Funds	Prime Rate	AAA only		instant access	£3m
Tier 6	Deposit/Call Account	HSBC			Instant access	£3m
	Call accounts	Santander group HBOS group RBS group			Call accounts with instant access	£3m less value of term deposits

**Nb** HM Treasury Credit Guarantee Scheme gives access to liquidity, if required, by Eligible Institutions.

The Sector colour coding suggests time limits of Green (3 months), Orange (6 months), red (1 year), purple (2 yrs) and blue (1 year).

The Credit Guarantee Scheme gives access to eligible institutions to liquidity from HM Treasury.