OVERVIEW AND SCRUTINY (ECONOMIC WELL-BEING) **11 NOVEMBER 2010**
CABINET **18 NOVEMBER 2010**
COUNCIL **15 DECEMBER 2010**

TREASURY MANAGEMENT
REVIEW OF PERFORMANCE
(Report by the Head of Financial Services)

1. INTRODUCTION

1.1 In February the Council adopted the latest edition of the *CIPFA Treasury Management in the Public Services: Code of Practice*, which requires the full Council to approve a treasury management strategy before the start of each financial year and to receive a mid-year report and an annual report after the end of the year. This is the first mid-year report presented under this Code and covers the period 1st April to 30th September 2010.

1.2 In addition, the DCLG *Guidance on Local Government Investments* recommends that local authorities review their investment strategy in the light of any changes in internal or external circumstances.

1.3 This report meets the requirements of both sets of guidance by reviewing the strategy, updating the Council on the performance of investments, and identifying any concerns over the credit-worthiness of counterparties.

2. TREASURY MANAGEMENT ACTIVITY

2.1. In December 2008, £10M was borrowed for 50 years to fund, in advance, part of the future capital programme thus taking advantage of very attractive long term rates available at the time. This sum was then invested for the remainder of the, then, MTP period pending its use for funding capital projects. Since that time long term rates have risen whilst short term rates have continued to be very low. Given the Council's financial challenges over the next few years it is therefore appropriate, for the present, to use the Councils own revenue reserves, supplemented by mostly short term borrowing, to temporarily fund the capital programme pending the return to a more "normal" interest rate structure.

2.2 Therefore, during the last 6 months most activity has been managing short term fluctuations in cash flow by borrowing or investing for short periods. However £7.5M has been invested for up to 9 months to take advantage of higher interest rates.

2.3 Much of the activity has been in liquidity accounts where the funds are accessible without notice, thus providing more security than term deposits, but also providing a good (in relative terms!) rate of return. For example, £3m was invested with Cambridge Building Society in August at 1.25% which was comparable to a nine month fixed rate deposit.

2.4 There have also been deficits at some points which have required the Council to borrow temporarily from other Local Authorities at low rates and for less than a month.

2.5 The following table summarises the transactions during the period:

		£m
Investments	- as at 31st March 2010	20.4
	- matured in period	-64.8
	- arranged in period	73.4
	- as at 30th Sept 2010	29.0
Borrowing	- as at 31st March 2010	-14.6
	- matured/repaid in period	34.2
	- arranged in period	-31.2
	- as at 30th Sept 2010	-11.6
Net investments at 31st March 2010		**5.8**
Net investments at 30th September 2010		**17.4**

2.6 The rise in net investments from April to September reflects the fact that the Council Tax is predominantly collected in 10 monthly instalments from April to January thus giving an improving cash flow from mid-April to mid-January each year.

2.7 On 30 September 2010 the Council had investments of £29M and borrowing of £11.6M. Annex A gives the details.

2.8 There are no current concerns about any of the investment counterparties.

3. PERFORMANCE SUMMARY

3.1 CDCM

In September 2010 the last investment managed by CDCM matured; this ended a relationship with this Fund Manager which goes back more than 10 years. The Council has benefited from the investments because they were made when rates were higher than at present. The return on these investments until September is 2.57% compared with the benchmark of 0.35%

3.2 **In-house funds**

The in-house portfolio historically comprised of a mixture of short-term investments and temporary borrowing to manage cash flow but now temporarily includes the borrowing and investment of the £10m advance borrowing from the PWLB. A performance of 1.41% compared with the benchmark of 0.2% has been achieved in the half-year

PERFORMANCE FOR THE 6 MONTHS APRIL 2010 – SEPTEMBER 2010					
	Performance (for half year)	Benchmark (for half year)	Variation from benchmark	Managed Funds	
				1 April 10	30 Sept 10
CDCM *	**2.59**%	0.35%*	**+2.23**%	£5.0m	0
In-house – investments net of borrowing **	**1.16**%	0.20%**	**+0.96**%	£0.8m	£17.4m
Net Investments				**£5.8m**	**£17.4m**

* 3 month LIBID ** 7 day rate

4. PERFORMANCE AGAINST BUDGET IN 2010/11

4.1 The latest forecast outturn is an increase in investment interest on the net budget (investment interest less borrowing costs) of £130k. The original budget was £199k

5. TREASURY MANAGEMENT STRATEGY

5.1 All treasury management activity undertaken during the period complied with the approved strategy, the *CIPFA Code of Practice*, and the relevant legislative provisions

5.2 There are no recommendations about changing the Strategy given the current and expected continuation of the interest rate structure that existed when it was approved and the existing emphasis on the security of counterparties.

6. COST OF BORROWING

6.1 As part of the Comprehensive Spending Review the Government announced an increase in the PWLB rates. Previously the rates to Local Authorities were 15 basis points (0.15%) above the cost of government borrowing (gilts); this margin was increased to an average of 100 basis points (1%) above the price of gilts which has resulted in a permanent increase in the cost of borrowing.

6.2 The impact on the revenue budget from the future increase in borrowing costs is partially offset by reduced minimum revenue provision (MRP).

6.3 Your Officers are working with the Council's Treasury Management Advisors to investigate opportunities for long-term borrowing from the market rather than PWLB.

7 TREASURY MANAGEMENT INDICATORS

7.1 The Council measures its exposures to treasury management risks using the following indicators. Council is asked to note the following indicators as at 30th September 2010.

7.2 **Interest rate exposures**

This indicator is set to control the Council's exposure to interest rate risk. The exposure to fixed and variable rate interest rates is based on the amount of net borrowing.

	Limit	Actual		
		Borrowing	Investment	Net
	£000	£000	£000	£000
Upper limit on fixed rate exposures (>12 months)	**35,100**	**10,000**	**-10,000**	**0**
Upper limit on variable rate exposures:				
. Fixed rates but < 12months		1,500	-16,500	-15,000
Variable		100	-2,500	-2,400
	3,775	**1,600**	**-19,000**	**-17,400**

The limits set by the Council in February 2010 were based on the understanding that investment or borrowing at a fixed rate, even if for a short duration, was still treated as fixed rate. It has now been clarified that arrangements of less than 12 months count as variable rate.

In the circumstances it is proposed to change the limits as follows in order to maximise the flexibility to react to the perceived direction of change in interest rates in the short, medium and long term.

	Limit £000
Upper limit on fixed rate exposures >12 months	+/- 35,100
Upper limit on variable rate exposures	+/- 35,100

7.3 **Maturity structure of borrowing**

This indicator is set to control the Council's exposure to refinancing risk. The maturity structure of fixed rate borrowing was:

Cash flow borrowing	Upper Limit	Lower Limit	Actual
Under 12 months	100%	100%	100%
Above 12 months	0%	0%	0%

Borrowing to fund capital schemes	Upper Limit	Lower Limit	Actual
Under 12 months	25%	0%	0%
12 months and within 24 months	25%	0%	0%
24 months and within five years	25%	0%	0%
Five years and within 10 years	50%	0%	0%
10 years and above	100%	0%	100%

7.4 **Investment repayment profile – limit on the value of investments that cannot be redeemed within 364 days**

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments.

The total principal sums invested to final maturities beyond the period end were:

	2010/11 £000	2011/12 £000	2012/13 £000
Limit on principal invested beyond year end	42,700	31,400	25,300
Actual principal invested beyond year end	10,000	10,000	5,000

8. RECOMMENDATIONS

8.1 Cabinet is requested to recommend to Council that it notes this report

BACKGROUND PAPERS
Working papers in Financial Services

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ANNEX A

Investments as at 30 September 2010

		£000	Investment date	Rate %	Repayment date
Term Deposits					
Royal Bank of Scotland	Temporary investment of PWLB borrowing	5,000	19/12/08	4.04	19/12/12
Skipton Building Society		5,000	19/12/08	4.85	19/12/13
Nottingham Building Society		2,500	24/2/10	2.22 #	23/2/11
Lloyds TSB		2,500	24/2/10	1.80	24/2/11
Lloyds TSB		2,500	17/5/10	1.40	17/2/11
Kent Reliance Building Society		2,500	16/8/10	1.30	17/3/11
Newcastle Building Society		2,500	16/8/10	1.38	17/3/11
Liquidity Accounts					
Cambridge Building Society		3,000	16/8/10	1.25	call
Alliance Leicester		800	1/9/10	0.80	call
NatWest		2,750	1/9/10	0.80	call
TOTAL		**29,050**			

Rate fixed for 3 months

Borrowing as at 30 September 2010

	£000	Borrowing date	Rate %	Repayment date
Long Term				
PWLB	5,000	19/12/08	3.91	19/12/57
PWLB	5,000	19/12/08	3.90	19/12/58
Short Term				
Thurrock Borough Council	800	28/9/10	0.52	15/10/10
Caerphilly County Borough Council	700	8/9/10	0.28	28/10/10
Brampton Parish Council *	100	1/4/10	0.50	
TOTAL	**11,600**			

* From the scheme whereby Parish Councils can deposit funds with the District