OVERVIEW AND SCRUTINY	**3 NOVEMBER 2011**
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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 second mid-year report presented under this Code and covers the period 1st April to 30th September 2011.

1.2 In addition, the Communities and Local Government *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 STRATEGY

2.1 The Council approved the 2011/12 treasury management strategy at its meeting on 23 February 2011.The investment strategy is to invest any surplus funds in a manner that balances low risk of default by the borrower with a fair rate of interest. The Council’s borrowing strategy permits borrowing for cash flow purposes and funding current and future capital expenditure over whatever periods are in the Council’s best interests.

2.2 It can be reported that all treasury management activity undertaken during the period complied with the approved strategy, the *CIPFA Code of Practice*, and the relevant legislative provisions.

3. TREASURY MANAGEMENT ACTIVITY

3.1. Short-term investment rates continue to be very low whilst long-term borrowing rates are higher. 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.

3.2 Therefore, during the last 6 months most activity has been in managing short term fluctuations in cash flow by borrowing or investing for short periods. However £3M was invested for 5 months from April to September 2011 to take advantage of slightly higher interest rates.

3.3 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.

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

3.5 The following table summarises the transactions during the period:

		£m
Investments	- as at 31st March 2011	15.5
	- matured in period	-77.0
	- arranged in period	80.8
	- as at 30th Sept 2011	19.3
Borrowing	- as at 31st March 2011	-13.1
	- matured/repaid in period	32.6
	- arranged in period	-29.5
	- as at 30th Sept 2011	-10.0
Net investments at 31st March 2011		**2.4**
Net investments at 30th September 2011		**9.3**

3.6 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 improved cash flow from mid-April to mid-January each year.

3.7 On 30 September 2011 the Council had investments of £19.3M and borrowing of £10.0M. Annex A gives the details.

4. PERFORMANCE SUMMARY

4.1 **In-house funds**

All the treasury management funds are managed in-house. The 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.

4.2 The performance summary below, however, is based only on short-term investments and borrowing as that gives a truer comparison with the current benchmark of the 7 day rate.

PERFORMANCE FOR THE 6 MONTHS APRIL 2011 – SEPTEMBER 2011					
	Performance	Benchmark	Variation from benchmark	Managed Funds	
				1 April	30 Sept
Net investments	0.73%	0.22%	+0.51%	£2.4m	£9.3m

5. PERFORMANCE AGAINST BUDGET IN 2010/11

5.1 The latest forecast outturn is for net investment interest to exceed the budget of £93k by £23k.

6. TREASURY MANAGEMENT STRATEGY

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

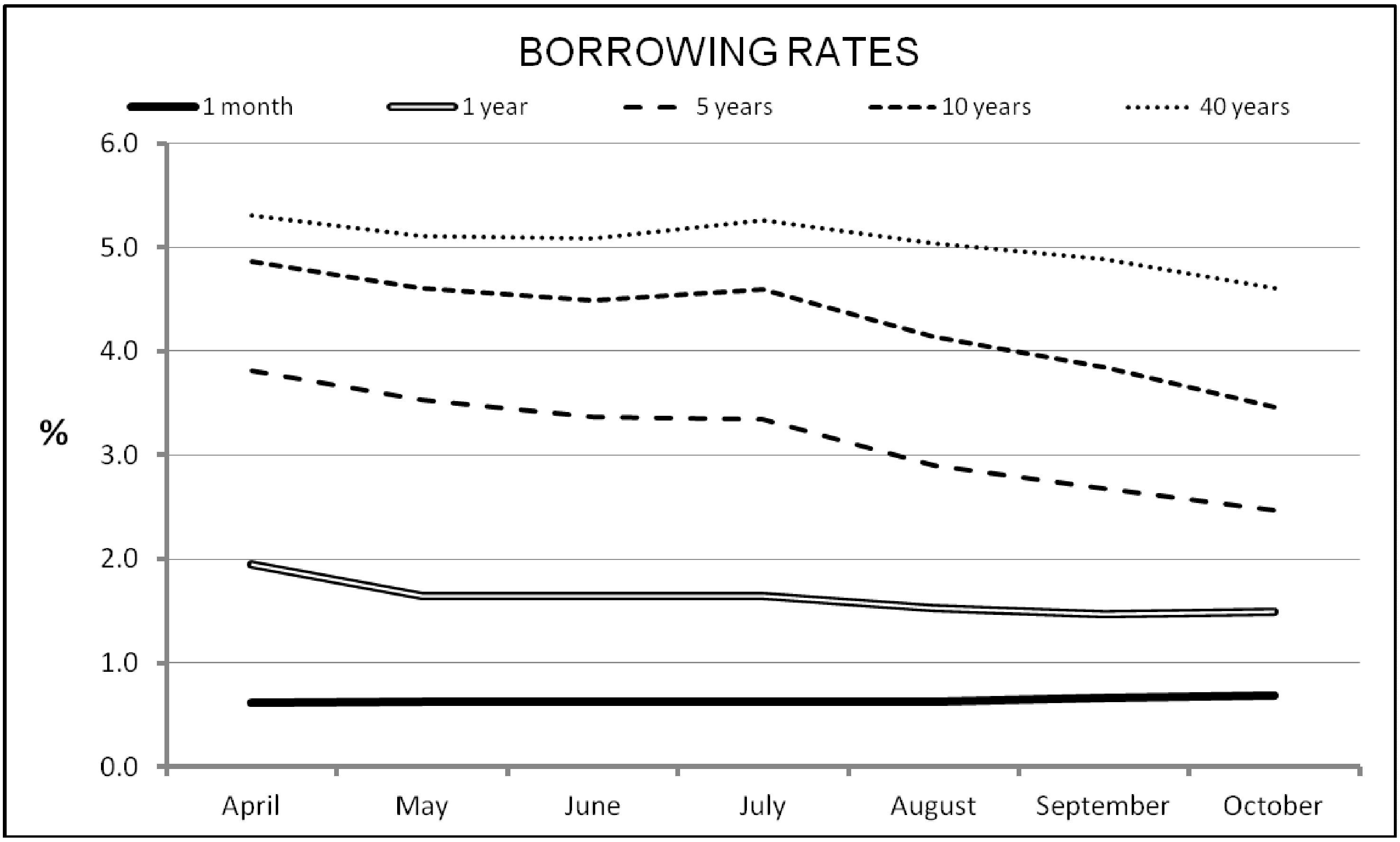
6.2 On 7 October 2011 Moody's, one of the leading credit Agencies, signalled the continuing international uncertainty by downgrading the long-term ratings of four banks and eleven building societies although their short-term ratings remained the same. They also considered which Building Societies the Government would be most likely to provide financial support to.

6.3 The Council has an investment of £5M with Skipton Building Society which matures in December 2013, and this is one of the societies which Moody's consider would be unlikely to receive Government Support if it got into difficulties. It is not felt that the Council's funds are particularly at risk though for a number of reasons. These include:

- The structure of Building Societies whereby wholesale depositors (e.g. HDC) have priority over retail deposits (the public).
- The ability of the building society industry to self-regulate by merging societies e.g. Chelsea and Stroud & Swindon in 2010 and Norwich & Peterborough in 2011.
- The high proportion of loans that are covered by assets.
- They are the 4th largest Society with assets of £13.7billion, reserves of £820 million and higher liquid assets (28%) than any of the top 12 Societies.

6.4 There is no need to amend the 2010/11 strategy due to these continuing international problems because it already allows us to minimise borrowing, thus reducing our levels of investments and to focus those investments into, no notice, liquidity accounts or shorter term time deposits. The Treasury Management Team is also investigating other investment opportunities such as AAA rated money market funds.

6.5 The chart below highlights the benefits of borrowing for short periods at the current time:



7 **TREASURY MANAGEMENT INDICATORS**

7.1 The Council measures its exposures to certain treasury management risks with the following indicators which generally relate to the position as at 30 September.

7.2 **Interest rate exposures**
This indicator is set to control the Council's exposure to interest rate risk. The calculation sets off fixed rate investments (£10M) against fixed rate borrowing (£10M) leaving the remaining short term investments all defined as variable.

	Limit	Actual
Upper limit on fixed rate exposures	**100%**	**0%**
Upper limit on variable rate exposures (all items on fixed rates for less than 12 months are defined as variable)	**100%**	**100%**

7.3 **Maturity structure of borrowing**
Following advice from our Treasury Management Advisers it is proposed to combine the two cash flow tables set in the original policy because of the difficulty of differentiating cash flow borrowing when it is in the Council's interest to use its own funds or to borrow short to cover capital

expenditure:

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

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

The **Proposed** replacement table and targets becomes:

Borrowing	Upper Limit	Lower Limit	Actual
Under 12 months	75%	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:

	2011/12 £000	2012/13 £000	2013/14 £000
Limit on principal invested beyond year end	18,700	13,100	10,100
Actual principal invested beyond year end	10,000	5,000	0

8. RECOMMENDATIONS

8.1 Cabinet is requested to recommend to Council:

- that it approves the revised table and targets in paragraph 7.3
- notes the contents of this report

BACKGROUND PAPERS

Working papers in Financial Services

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ANNEX A

Investments as at 30 September 2011

		£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
Bank of Scotland		5,000	11/03/11	1.93	08/02/12
Liquidity Accounts					
Cambridge Building Society		3,000	15/09/11	1.25	call
NatWest		1,300	30/09/11	0.80	call
TOTAL		**19,300**			

Borrowing as at 30 September 2011

	£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				
None	0			
TOTAL	**10,000**			