Cabinet

Report of the meetings held on 17th May and 21st June 2012

Matter for Determination

1. **TREASURY MANAGEMENT ANNUAL REPORT 2011/2012**

By way of a report by the Head of Financial Services (attached as Document 1), the Cabinet has been acquainted with the performance in the investment of the Council's capital receipts for the year ending 31st March 2012.

The Council has continued to carry out its treasury management activities with due regard to minimising risk, and in accordance with the relevant legislation.

Having been acquainted with the deliberations of the Overview and Scrutiny (Economic Well-Being) Panel on this matter, as described in Item No. 2 of their Report, the Cabinet

RECOMMEND

> **that the Council receives the Treasury Management Annual Report 2011/12 and approves the amended Appendix B of the Treasury Management Strategy for 2012/13 reproduced as Document 2.**

Matters for Information

2. **APPOINTMENT OF EXECUTIVE COUNCILLORS**

Executive responsibilities for the Municipal Year 2012/13 have been allocated by the Executive Leader of the Council as follows:-

- Strategic Economic Development - Councillor J D Ablewhite
- Strategic Planning and Housing - Councillor N J Guyatt
- Healthy and Active Communities - Councillor T D Sanderson
- Resources - Councillor J A Gray
- Environment - Councillor D M Tysoe
- Customer Services -Councillor B S Chapman

Executive Councillors have been appointed to serve as ex-officio Members of Panels as follows –

Executive Councillor for	**Ex-Officio for**
Strategic Planning and Housing Healthy and Active Communities	Development Management Panel Licensing and Protection Panel/ Licensing Committee

The Executive Leader has been appointed ex-officio member of the Employment Panel.

3. REPRESENTATION ON ORGANISATIONS AND PARTNERSHIPS 2012/13

The Cabinet has made appointments/nominations in relation to representation on a variety of organisations/partnerships and has authorised the Head of Legal and Democratic Services, after consultation with the Deputy Executive Leader of the Council, to make any changes that may be required throughout the year.

4. EQUALITY FRAMEWORK FOR LOCAL GOVERNMENT EQUALITY PEER CHALLENGE – ACHIEVING ACCREDITATION

In conjunction with the Overview and Scrutiny Panel (Social Well-Being) and the Employment Panel, Item Nos 1 and 5 of their Reports refer, the Cabinet has noted the accreditation obtained by the Council as an "Achieving" authority under the Equality Framework for Local Government. The Framework is a performance improvement and benchmarking tool which is designed to help local government meet their legal equality duties.

In considering the key findings of the assessment, Executive Councillors have noted that the areas identified for future consideration will be progressed by way of an action plan which includes issues regarding future growth, service equity, engagement and staff communication.

J D Ablewhite
Chairman

TREASURY MANAGEMENT ANNUAL REPORT 2011/12
(Report by the Head of Financial Services)

1. INTRODUCTION

1.1 Council approves the Treasury Management strategy for the forthcoming year when it approves the budget and MTP each February. It also receives a mid-year report and an annual report after the end of the financial year. The Council's Strategy also requires scrutiny of the Treasury Management function to be carried out by the Economic Well-being Panel.

1.2 The Council approved the 2010/11 treasury management strategy at its meeting on 17th February 2011. The key points were:

- to invest any available funds in a manner that balanced low risk of default by the borrower with a fair rate of interest.
- to ensure it had sufficient cash to meet its day-to-day obligations
- to borrow when necessary to fund capital expenditure and to borrow in advance if rates were considered to be low. It envisaged the need for further borrowing in the range of £4.9M to £19.8M.

2. ECONOMIC REVIEW

2.1 The Eurozone debt crisis dominated the financial year 2011/12. The apparent inability of leaders to either agree on remedial policies or implement fiscal consolidation measures prompted frequent bouts of market volatility, exacerbated by multiple sovereign rating downgrades, as investors positioned themselves for potential government defaults or even the breakup of the Eurozone itself.

2.2 Exposure to the Eurozone periphery and new regulations aimed at reducing the need for government support created downward pressure on the creditworthiness of many European banks, prompting a raft of credit rating downgrades. The European Central Bank (ECB) pulled the Eurozone back from the brink in late December by cutting interest rates and providing cheap long-term loans, immediately reducing the near-term risk of a liquidity crisis and temporarily calming financial markets.

2.3 The UK's reliance on the Eurozone as a major trading partner was illustrated when it followed the Eurozone into recession over the last six months of the financial year. Other factors responsible for the fall in economic activity included the government's deficit reduction programme and the weakness in household and business spending. The decline in household spending was the result of low confidence and the erosion of disposable income by persistently elevated inflation, subdued wage growth, higher taxes and rising unemployment. Businesses were in a similarly weak position, with access to credit restricted or too expensive due to a risk-averse banking sector, and subdued domestic and foreign demand.

2.4 Weakening economic growth and signs of further deterioration in the Eurozone prompted the Bank of England to loosen monetary policy in October, despite above target inflation. With Bank Rate already at 0.5%, the Monetary Policy Committee (MPC) voted for a further £50bn of quantitative easing which helped push gilt yields to record lows over the following few months. Policymakers justified the action because they were confident inflation would fall quickly back to target during 2012. However, although the annual Consumer Price Index (CPI) rate declined from the September peak of 5.2%, a combination of higher crude oil and food prices caused the rate to rise slightly in March to 3.5%, leaving Bank of England policymakers in the unenviable position of setting policy to battle both weak growth and high inflation.

3. PERFORMANCE OF FUNDS

3.1 The following table summarises the treasury management transactions undertaken during the 2011/12 financial year and the details of the investments and loans held as at 31 March 2012 are shown in Annex A.

	Principal Amount £m	Interest Rate %
Investments		
at 31st March 2011	15.5	3.50
less matured in year	-161.0	
plus arranged in year	+155.9	
at 31st March 2012	10.4	4.29
Average Investments	**20.1**	**2.90**
Borrowing		
at 31st March 2011	13.1	3.13
less repaid in year	-37.4	
plus arranged in year	+38.8	
at 31st March 2012	14.5	2.82
Average Borrowing	**12.3**	**3.23**

3.2 The average rate of interest on investments of 2.9% was 2.5% above the 7-day benchmark rate of 0.4% This very good performance was due to £10m of the investments being locked into higher rates before the year started together with the use of liquidity accounts with major banks and building societies which gave the added safety of instant access together with interest rates comfortably in excess of the benchmark.

3.3 The Council's exposure to interest rate risk at the end of the year was the £10M long term PWLB borrowing from 3 years ago which is still well below current long term rates and £4.5M short term borrowing for less than 3 weeks at a mixture of 0.3% and 0.5%. This gave an average borrowing rate of 3.23%.

3.4 The actual net investment interest (after deduction of interest payable on loans) was a credit of £183k compared with a credit budget of £93k due to the higher than estimated interest rates and higher levels of reserves.

4. STRATEGY – BORROWING

4.1 Long-term borrowing. The strategy allowed for 'must borrow' to finance that part of the capital programme that could not be met from internal funds. There was also a provision for 'may borrow' which allowed borrowing in anticipation of need, based on whether longer term rates seemed low compared with future likely levels. No long-term borrowing was carried out as the rates were not deemed to be low enough, short-term borrowing rates were very low, and for most of the year much of the funding need was covered by internal funding.

4.2 Short-term borrowing. The Authority needed to borrow short-term during the year to manage its cash flow; it averaged £2.3m.

5. STRATEGY - INVESTMENTS

5.1 The Council's strategy for 2011/12 was based on all investments being managed in-house. The investments were of two types, time deposits and liquidity (call) accounts with banks with a high credit rating and the top 25 building societies by asset value. The strategy included limits on the size of investments with each organisation and country limits. The limits are shown in Annex B**.**

5.2 The strategy was reviewed during the course of the year with the Treasury Management Advisory Group, which re-confirmed their comfort with investments in building societies.

5.3 The Authority arranged a facility to invest in a AAA money market fund, as an alternative to using liquidity accounts. However as at 31 March 2012 it had not been used as a higher return was obtained from the liquidity accounts.

6. RISK MANAGEMENT

6.1 The Council's primary objectives for the management of its investments are to give priority to the security and liquidity of its funds before seeking the best rate of return.

6.2 **Security** is managed by investing short-term with highly-rated banks, building societies and local authorities in the UK. The Authority receives regular updates from its advisors, Sterling Consultancy Services, sometimes daily, on changes to the credit rating of counterparties. This allows the Council to amend its counterparty list and not invest where there is concern about the credit rating.

6.3 **Liquidity.** The Authority has £10m invested in time deposits since December 2008 and due for repayment, £5m in December 2012 and £5m in December 2013, but otherwise the majority of the funds are in liquidity accounts which have a rate or interest above base rate and provide instant access to funds.

6.4 Overall, liquidity is managed by producing cash flow forecasts that help set the limit on the duration of the investments in time deposits. The projections tend to be cautious which sometimes resulted in funds being available before they were needed with any surplus easily being invested on a temporary basis.

6.5 **Return on investments.** Security and liquidity take precedence over the return on investments, which has resulted in investments during 2011/12 generally being of short duration due to the benefit of good rates on liquidity and growing concerns over the credit rating of counterparties.

6.6 When the Authority borrowed £10M in advance in December 2008 it invested the funds at marginally higher interest rates thus protecting the Council from any short term loss of interest.

7. COMPLIANCE WITH REGULATIONS AND CODES

7.1 All the treasury management activity undertaken during the financial year complied with the approved strategy, the CIPFA Code of Practice, and the relevant legislation

7.2 The Code requires the Council to approve Treasury Management and Prudential Indicators. Those for 2011/12 were approved at the Council meeting on 17th February 2011. Annex C shows the relevant indicators and the actual results.

8 CONCLUSION

8.1 The performance of the funds in a year when rates stayed very low was pleasing, significantly exceeding both the benchmark and the budgeted investment interest.

8.2 In a year of uncertainty in the financial markets all of the Council's investments were repaid in full and on time.

8.3 The Authority has carried out its treasury management activities with due regard to minimising risk, and in accordance with legislation. During the year it reviewed its strategy in the light of external events in the markets.

9 RECOMMENDATION

9.1 It is recommended that Cabinet note this report.

BACKGROUND INFORMATION
2011/12 cash management files and working papers
Reports to the Cabinet and Treasury Management Advisory Group
CIPFA Code on Treasury Management

CONTACT OFFICER
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ANNEX A

BORROWING AND INVESTMENTS AT 31 MARCH 2012

	SHORT-TERM RATING FITCH	SHORT-TERM RATING MOODY'S	DATE INVESTED/ BORROWED	AMOUNT £M	£M	INTEREST RATE %	REPAYMENT DATE	YEAR OF MATURITY
BORROWING								
Short term								
Coventry City Council			19-Mar-12	-2.0		0.30	18-Apr-12	2012/13
Shropshire Council			14-Mar-12	-2.5		0.50	20-Apr-12	2012/13
					-4.5			
Long term								
PWLB			19-Dec-08	-5.0		3.91	19-Dec-57	2057/58
PWLB			19-Dec-08	-5.0		3.90	19-Dec-58	2058/59
					-10.0			
TOTAL BORROWING					**-14.5**			
INVESTMENTS								
IN-HOUSE								
Short term								
Natwest Liquidity Account	F1	P1		0.3		0.80		2012/13
Cambridge Building Society	Not rated			0.1		1.25		2012/13
					0.4			
Medium term								
Royal Bank of Scotland	F1	P1	19-Dec-08	5.0		4.04	19-Dec-12	2012/13
Skipton Building Society	F3		19-Dec-08	5.0		4.85	19-Dec-13	2013/14
					10.0			
TOTAL - INVESTMENTS					**10.4**			
NET BORROWING					**-4.1**			

IN-HOUSE FUND MANAGEMENT 2011/12
(IF NO FURTHER BORROWING IN ANTICIPATION)

<table>
<tr><td>Duration of investments</td><td>No investment shall be longer than 5 years.
Maximum duration for a Building Society with a rating of BBB+ or lower, or no credit rating, is 6 months</td></tr>
<tr><td>Types of investments</td><td>Fixed term Deposits
Deposits at call, two or seven day notice
Corporate bonds
Money market funds</td></tr>
<tr><td>Credit Ratings</td><td>Excluding Building Societies
Short term rating F1 by Fitch or equivalent)
Long-term rating of AA- by Fitch or equivalent if the investment is longer than 1 year.</td></tr>
<tr><td>Maximum limits per counterparty (group), country or non-specified category</td><td>
<table>
<tr><td>F1+ or have a legal position that guarantees repayment for the period of the investment</td><td>£5M</td></tr>
<tr><td>F1</td><td>£4M</td></tr>
<tr><td>Building Society with assets over £2bn in top 25 (Currently 10)</td><td>£5M</td></tr>
<tr><td>Building Society with assets over £1bn if in top 25 (Currently 3)</td><td>£4M</td></tr>
<tr><td>Building Society with assets under £1bn in top 25</td><td>£3M</td></tr>
<tr><td>Liquidity (Call) Account with a credit rating of F1+ or with a legal position that guarantees repayment or a Building Society.</td><td>£5M</td></tr>
<tr><td>BUT total invest with counterparty/group shall not exceed</td><td>£8M</td></tr>
<tr><td>Money market fund AAA Credit rating</td><td>£4m</td></tr>
</table>
Limit for Non-specified investments
– £10M in time deposits more than one year
– £5M in corporate bonds
– £10M in total

Country limits
– UK - unlimited
– £5M in a country outside the EU
– £10M in a country within the EU (excluding UK)
– £20M in EU countries combined (excluding UK)

These limits will be applied when considering any new investment from 23 February 2011. Lower limits may be set during the course of the year or for later years to avoid too high a proportion of the Council's funds being with any one counterparty.</td></tr>
<tr><td>Benchmark</td><td>LGC 7 day rate</td></tr>
</table>

Annex C

Prudential Indicators for 2011/12 relating to Treasury Management
Comparison of actual results with limits

EXTERNAL DEBT

The authorised limit for external debt.
This is the maximum limit for borrowing and is based on a worst-case scenario. This limit, and the operational boundary below, were set to allow up to £36.5m of borrowing in anticipation of need.

2011/12 Limit £000	**2011/12 Actual £000**
65,000	**15,100**

The operational boundary for external debt.
This reflects a less extreme position. Although the figure can be exceeded without further approval it represents an early warning monitoring device to ensure that the authorised limit (above) is not exceeded.

2011/12 Limit £000	**2011/12 Actual £000**
60,000	**15,100**

Both of these actual results reflect the fact that long term rates were not considered low enough to borrow in anticipation of need

TREASURY MANAGEMENT

Exposure to investments with fixed interest and variable interest.
These limits are given as a percentage of total investments. Investments of less than 12 months count as variable rate.

	2011/12 Limit	**2011/12 Actual as at 31.3.12**
Upper limit on fixed rate exposure	100%	**96%**
Upper limit on variable rate exposure	100%	**4%**

Borrowing Repayment Profile
The proportion of 2011/12 borrowing that matured in successive periods.

Borrowing	Upper limit	**Actual As at 31.3.12**	Lower limit
Under 12 months	75%	31%	0%
12 months and within 24 months	25%	0%	0%
24 months and within 5 years	25%	0%	0%
5 years and within 10 years	50%	0%	0%
10 years and above	100%	69%	0%

Investment Repayment Profile
Limit on the value of investments that cannot be redeemed within 364 days.

2011/12 Limit £000	**2011/12 Actual - maximum in year £000**	**2011/12 Actual as at 31.3.12 £000**
18,700	**10,000**	**5,000**

APPENDIX B (Document 2)

IN-HOUSE FUND MANAGEMENT (IF NO FURTHER ADVANCE BORROWING)

Duration of investments	No investment shall be longer than 5 years. Maximum duration for a Building Society with no rating is 1 month.
Types of investments	Fixed term Deposits Deposits at call, two or seven day notice Corporate bonds Money market funds UK Government bonds and Supranational Bank bonds.
Credit Ratings	**Building Societies** All Building Societies with ratings of BBB or above. Building Societies with no ratings. **Money Market Funds** AAA credit rating **Local Authorities or UK Government** No rating required **Non-Building Societies** Short term rating F1 by Fitch or equivalent. **Short term rating F2 by Fitch or equivalent for liquidity accounts** Long-term rating of AA- by Fitch or equivalent if the investment is longer than 1 year.
Maximum limits per counterparty (group), country or non-specified category	F1+ or have a legal position that guarantees repayment for the period of the investment — £5M F1 — £4M Building Society with assets over £2bn in top 25 (Currently 10) — £5M Building Society with assets over £1bn if in top 25 (Currently 3) — £4M Building Society with assets under £1bn in top 25 — £3M Liquidity (Call) Account with a credit rating of **F2** or with a legal position that guarantees repayment or a Building Society. — £5M BUT total invested with counterparty/group shall not exceed — £8M Money market fund AAA Credit rating — £4m **Limit for Non-specified investments** – £10M in time deposits more than one year – £5M in corporate bonds – £10M in any other types. – £15M in total **Country limits** – UK - unlimited – £5M in a country outside the EU – £10M in a country within the EU (excluding UK) – £20M in EU countries combined (excluding UK) No investment will be made in country with a sovereign rating of less than AA. These limits will be applied when considering any new investment from 23 February 2012. Lower limits may be set during the course of the year or for later years to avoid too high a proportion of the Council's funds being with any counterparty.
Benchmark	LGC 7 day rate