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TREASURY MANAGEMENT OUTTURN 2012/13

EXECUTIVE MEMBER:	Councillor Gillian Troughton
LEAD OFFICER:	Darienne Law, Head of Corporate Resources
REPORT AUTHOR:	Leanne Barwise – Senior Accounting Officer

Why has this report come to the Executive?

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2012/13. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

Recommendations:

The Executive are asked to make a recommendation to Council to:

(i) Approve the actual 2012/13 prudential and treasury indicators attached at Appendix A.

(ii) Note the Treasury Management Outturn 2012/13 detailed in Section 9 of this report.

(iii) Note the make-up of the portfolio of investments as at 31st March 2013 attached at Appendix B.

(iv) Note that this report will be formally considered by the Audit Committee on 26th June prior to being approved by Council on 12th September 2013.

1. Introduction

Changes in the regulatory environment place a much greater onus on Members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by Members.

During 2012/13 the minimum reporting requirements were that the full Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 23rd February 2012)
- a mid-year (minimum) treasury update report (Council 13th November 2012)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

In addition, this Council has received quarterly treasury management update reports on 21st August 2012 and 12th February 2012 which were presented to Executive.

This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to the reports by the Audit Committee before being reported to Council (wherever possible). This report will be presented to Audit Committee on 26th June prior to being considered by Council on 12th September 2013.

Member training on treasury management issues was undertaken prior to Audit Committee on 31st January 2013 in order to support Members' scrutiny role. Another annual training session will be arranged for the 2013/14 financial year as part of the ongoing Treasury Management training program for Members and Officers.

2. The Economy and Interest Rates

The financial year 2012/13 continued the challenging investment environment of previous years, namely low investment returns and continuing heightened levels of counterparty risk. The original expectation for 2012/13 was that Bank Rate would start gently rising from quarter 4 2014. However, economic growth in the UK was disappointing during the year due to the UK austerity programme, weak consumer confidence and spending, a lack of rebalancing of the UK economy to exporting and weak growth in our biggest export market - the European Union (EU). The UK coalition Government maintained its tight fiscal policy stance against a background of warnings from two credit rating agencies that the UK could lose its AAA credit rating. Key to retaining this rating will be a return to strong economic growth in order to reduce the national debt burden to a sustainable level, within the austerity plan timeframe. Weak UK growth resulted in the Monetary Policy Committee increasing quantitative easing by £50bn in July to a total of £375bn. Bank Rate therefore ended the year unchanged at 0.5% while CPI inflation peaked fell from 3% at the start of the year to end at 2.8% in March, with a fall back to below 2% pushed back to quarter 1 2016. The EU sovereign debt crisis was an ongoing saga during the year with first Greece and then Cyprus experiencing crises which were met with bailouts after difficult and fraught negotiations.

Gilt yields oscillated during the year as events in the ongoing Eurozone debt crisis ebbed and flowed, causing corresponding fluctuations in safe haven flows into / out of UK gilts. This, together with a further £50bn of QE in July and widely expected further QE still to come, combined to keep PWLB rates depressed for much of the year to historically very low levels.

Deposit rates. The Funding for Lending Scheme, announced in July, resulted in a flood of cheap credit being made available to banks and this has resulted in money market investment rates falling sharply in the second half of the year. However, perceptions of counterparty risk have improved after the ECB statement in July that it would do "whatever it takes" to support struggling Eurozone countries. This has resulted in some return of confidence to move away from only very short term investing.

3. Overall Treasury Position as at 31st March 2013

At the beginning and the end of 2012/13 the Council's treasury position was as follows:

	31st March 2012 Principal	Rate/ Return	Average Life (Years)	31st March 2013 Principal	Rate/ Return	Average Life (Years)
Total debt (Fixed rate funding)	*£5.00m*	*7.55%*	*30*	*£5.00m*	*7.55%*	*29*
CFR	*£8.88m*			*£8.45m*		
Over / (under) borrowing	*£3.23m*			*£3.23m*		
Total investments	*£18.92m*			*£18.45m*		
Net debt	*(£6.81m)*			*(£6.77m)*		

4. The Strategy for 2012/13

The expectation for interest rates within the strategy for 2012/13 anticipated low but rising Bank Rate (starting in quarter 4 of 2014) with similar gradual rises in medium and longer term fixed borrowing rates over 2012/13. Variable or short-term rates were expected to be the cheaper form of borrowing (if necessary) over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by the use of low risk counterparties, inevitably resulting in relatively low returns.

The strategy remained relatively unchanged from the necessary revision in October 2011 which reflected the heightened uncertainty in the economic market at the time, which in turn is still reflective of the current economic climate. The tightened restrictions on our investment criteria remained and we utilised "safe havens" being UK semi-nationalised institutions (RBS & Lloyds/BOS Group) and placed investments with additional Money Market Funds (highly rated liquid institutions) or instant access accounts with Banks, in lieu of placing investments with Building Societies or lower rated counterparties. This ensured there was a balance between security and liquidity of funds and the yield achieved, with security being the principle concern particularly in the current economic climate.

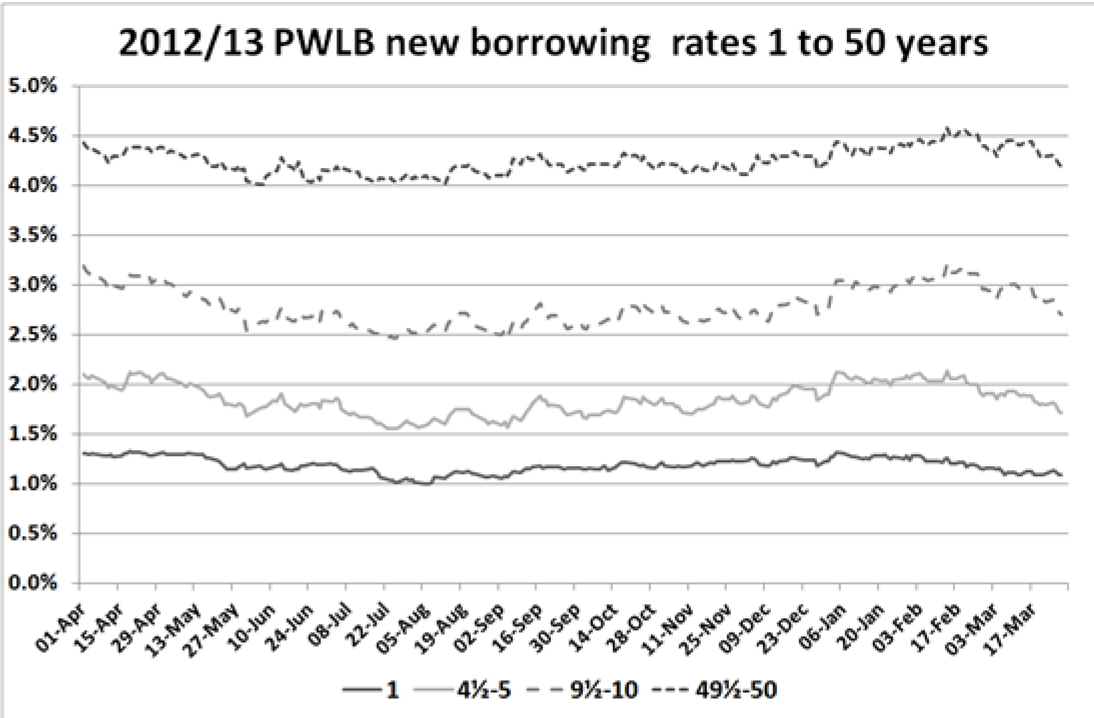
5. The Borrowing Requirement and Debt

The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR).

	31 March 2012 Actual	31 March 2013 Estimate	31 March 2013 Actual
Total CFR	£8.88m	£8.88m	£8.45m

6. Borrowing Rates in 2012/13

PWLB borrowing rates - the graph below shows how PWLB rates remained close to historically very low levels during the year.



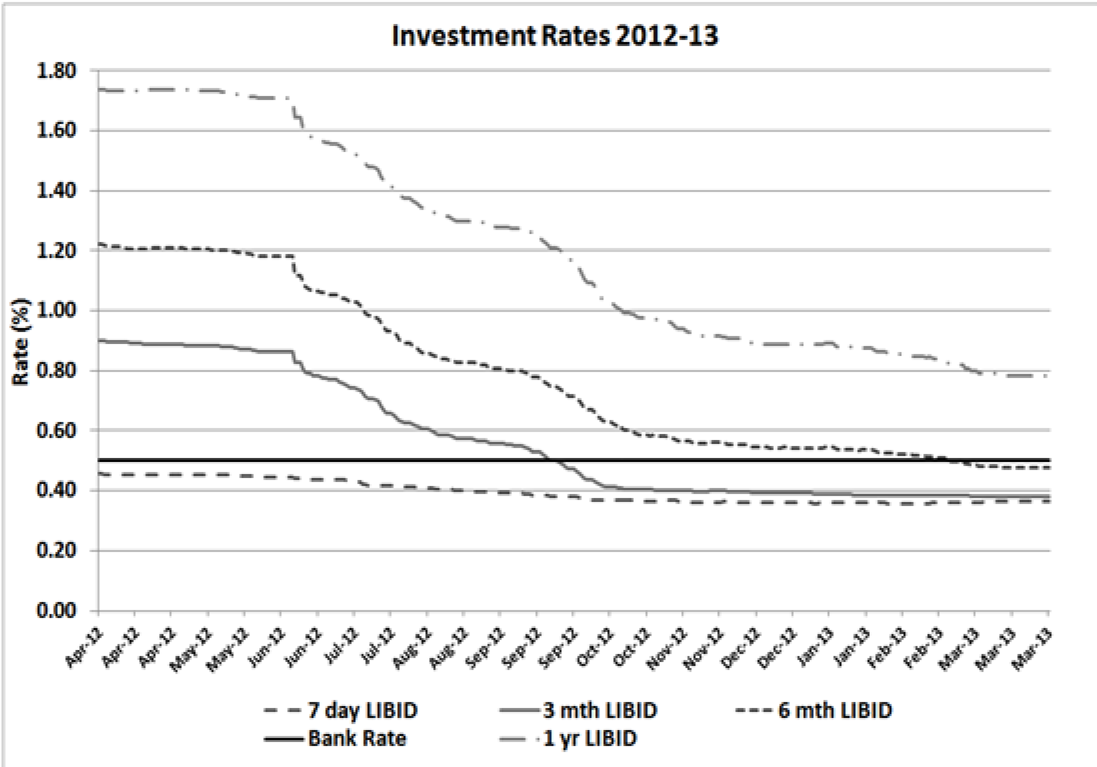
7. Borrowing Outturn for 2012/13

Borrowing – The Council only has one remaining market loan in its debt portfolio as detailed below. We continually assess the position of this loan with our Treasury Consultants, Sector, to ensure we are securing the best terms for the Council. At the current time, the advice is to leave the loan in its present form, as the penalty for repaying early would be prohibitive.

Lender	Principal	Date Advanced	Type	Interest Rate	Maturity	Date of Maturity
Market	£5.00m	01/02/2002	Fixed interest rate	7.55%	29 years	01/02/2042

8. Investment Rates in 2012/13

Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for four years. Market expectations of the start of monetary tightening were pushed back during the year to early 2015 at the earliest. The Funding for Lending Scheme resulted in a sharp fall in deposit rates in the second half of the year.



9. Investment Outturn for 2012/13

Investment Policy – the Council's investment policy is governed by CLG guidance, which was implemented in the annual investment strategy approved by the Council on 23rd February 2012. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc). Operationally, however, within the strategy we have temporarily restricted the use of Building Societies and other lower rated institutions and ensured funds are only placed with semi-nationalised institutions, higher rated banks or Money Market Funds and instant access accounts.

The Council had no liquidity difficulties and the investment activity during the year conformed to the approved strategy with the exception of the following:-

- An investment temporarily breached our self-imposed counterparty limit of £7.5m by £2,590 for a period of one day. This was due to interest being credited to the account and was rectified immediately.
- An investment that had matured was not automatically credited to our account due to complications in the banking system. When the funds were finally credited to our account we were unable to place another deal within the very limited banking deadlines and so the funds were placed overnight in our NatWest Special Interest Bearing Account (SIBA) at 0.5% and earned £370 in interest. The funds were transferred out to the Debt Management Account Deposit Facility (DMADF) the following day. This was an overnight breach of our self-imposed counterparty limit as NatWest is part of the Royal

Bank of Scotland (RBS) and we would normally reduce the balance within our NatWest Account to a minimum level to remain within these limits.

Investments held by the Council - Over the full financial year, the Council maintained an average balance of £25m of internally managed funds. The actual interest earned for 2012/13 was £288,585 (as reported in the Revenue Out-turn Report) against a budgeted return of £227,822, resulting in a net improvement against the budgeted return on investments for 2012/13 of £60,763. This compares to actual interest earned in 2011/12 of £267,565 against a budget estimate of £252,822, resulting in a small net improvement for 2011/12 of £14,743.

The actual interest received over the period has improved by £46,020 whilst bank base rates have stayed the same at 0.5%. This reflects the changes in the Treasury Management Investment Strategy implemented in October 2011 which enabled the Authority to place a greater amount of investment with the part nationalised banks to maximise returns at very favourable rates.

The internally managed funds earned an average rate of return of 1.15% over the 2012/13 financial year. This compares with a 2012/13 budget assumption of £25m investment balances earning an assumed interest rate of approximately 1.25% which was then adjusted for budget savings and/or pressures. In comparison the average rate of return achieved in 2011/12 of 1.08%.

10. Conclusion

The Council has complied with all of the relevant statutory and regulatory requirements which require the Council to identify and, where possible, quantify the levels of risk associated with its treasury management activities. In particular, its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach.

11. Statutory Officer Comments

11.1 The Monitoring Officer's comments are:

11.2 The Section 151 Officer's comments are: Included within this report

11.3 Other consultee comments, if any:

11.4 Policy Framework comments: The Treasury Management Strategy is a key component of the Council's overall policy framework and this report supports the management and delivery of the framework. The report further refers to the national and international policy framework in which the Council's Treasury Management Strategy is operating within.

12. How will the proposals be project managed and how are the risks going to be managed?

The Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
- The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken;
- Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act;
- The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;
- The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;
- Under the Act the CLG has issued Investment Guidance to structure and regulate the Council's investment activities.

Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices.

List of Appendices

Appendix A – Prudential & Treasury Indicators
Appendix B - Temporary Investments as at 31st March 2013

List of Background Documents: Treasury Management Strategy 2012/13, Mid-Year Treasury Management Report 2012/13, Capital Programme 12/13 – Outturn Report

Appendix A

Capital Prudential and Treasury Indicators

The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential code and produce prudential indicators. Each indicator either summarises the expected capital activity or introduces limits upon that activity, reflecting the outcome of the Council's underlying capital appraisal systems.

During 2012/13, this Council has complied with its legislative and regulatory requirements i.e. the Capital Prudential Indicators that were set at Full Council within the Treasury Management Strategy 2012/13 on 23rd February 2012. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

A. **Net borrowing and the CFR** - in order to ensure that borrowing levels are prudent over the medium term the Council's external borrowing, net of investments, must only be for a capital purpose. This essentially means that the Council is not borrowing to support revenue expenditure. Net borrowing should not therefore, except in the short term, have exceeded the CFR for 2012/13 plus the expected changes to the CFR over 2013/14 and 2014/15 from financing the capital programme. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2012/13. ***The Council has complied with this indicator as detailed within Table A overleaf.***

B. **The authorised limit** - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. The Council does not have the power to borrow above this level. ***Table B demonstrates that during 2012/13 the Council has maintained gross borrowing within our authorised limit.***

C. **The operational boundary** – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached. ***See Table B for the 2012/13 out turn position of the operational boundary.***

D. **Actual financing costs as a proportion of net revenue stream** - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

Table A

Actual prudential and treasury indicators	Ref	2011/12 Actual £m	2012/13 Original Estimate £m	2012/13 Actual £m
Capital expenditure		£2.25m	£2.16m	£1.52m
Capital Financing Requirement		£8.88m	£8.88	£8.45m
Net borrowing	(a-b)	(£6.85m)	(£3.23m)	(£6.09m)
External debt	(a)	£12.07m	£11.88m	£12.36m
Investments - Under 1 year	(b)	£18.92m	£15.11m	£18.45m

Table B

Prudential Indicator	2012/13
Authorised limit	£17.00m
Maximum gross borrowing position	£12.37m
Operational boundary	£12.00m
Average gross borrowing position	£12.11m
Financing costs as a proportion of net revenue stream	6.92%

Affordability Prudential Indicators

The previous tables cover the overall capital and control of borrowing prudential indicators, but we are also required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances.

The indicator detailed in Table C below, identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

Table C

Ratio of financing costs to net revenue stream	31 March 2012 Actual	2012/13 Original Limits	31 March 2013 Actual
	3.34%	7.03%	6.92%

The next indicator as detailed in Table D (below) identifies the revenue costs associated with proposed changes to the three year capital programme recommended at Full Council on 23rd February 2012 compared to the Council's existing approved commitments and current plans.

Table D

Incremental impact of capital investment decisions	31 March 2012 Actual	2012/13 Original Limits	31 March 2013 Actual
Increase in Council Tax (Band D) per annum	0%	0%	0%

The maturity structure of the debt portfolio was as follows:

	31 March 2012 Actual	2012/13 Original Limits	31 March 2013 Actual
Under 12 months	100%	100%	100%
12 months and within 5 years	100%	100%	100%
5 years and within 10 years	100%	100%	100%
10 years and within 20 years	100%	100%	100%
20 years and within 30 years	100%	100%	100%
30 years and within 40 years	100%	100%	100%
40 years and above	100%	100%	100%

All investments within the Councils portfolio were placed for under one year. The authority held 100% specified investments at the year-end against a maximum limit of 75% non-specified investments.

The exposure to fixed and variable rate investments was as follows:

	31 March 2012 Actual	31 March 2013 Actual
Fixed rate (Principal)	£7.50m	£7.40m
Variable rate (Principal)	£11.42m	£11.05m
TOTAL INVESTMENT	**£18.92m**	**£18.45m**

APPENDIX B

TEMPORARY INVESTMENTS AT 31st MARCH 2013

	AMOUNT	PERIOD OF LOAN	VALUE DATE	MATURITY DATE	RATE	BASE RATE
BANK OF SCOTLAND	7,490,000	CALL			0.75%	
RBS MMF	1,561,000	CALL			0.33%	
IGNIS MMF	2,000,000	CALL			0.40%	
RBS 95 DAY NOTICE	7,400,000	95 DAYS	11/01/2013	18/04/2013	1.25%	
TOTAL	**18,451,000**				0.88%	0.50%

SUMMARY

	BALANCE	LIMIT	AVAILABLE
BANK OF SCOTLAND/LLOYDS	7,490,000	10,000,000 *	2,510,000
RBS MMF	1,561,000	5,000,000	3,439,000
RBS	7,400,000	10,000,000 *	2,600,000
IGNIS MMF	2,000,000	5,000,000	3,000,000
INSIGHT MMF	0	5,000,000	5,000,000
BLACKROCK MMF	0	5,000,000	5,000,000
DMADF	0	UNLIMITED	UNLIMITED
	18,451,000	**40,000,000**	**21,549,000**

* Investment limit of £7.5m, however ulitmate limit of upto £10m with prior approval of S151 and for short term investments only.