

Audit Committee

6 December 2011

Report of the Head of Finance & property Services

ITEM 7 Treasury Outturn Report for 2010-11

Purpose of Report

To report to the Committee the Council's Treasury Management, Investment management and Prudential Code outturns for 2010-11.

Action Requested

That the contents of the report be noted.

Policy Context

That we will deliver value for money for the people of Charnwood Borough Council.

Background

The Council is required through regulations issued under the Local Government Act 2003 to produce an annual treasury report reviewing treasury management activities and the actual prudential and treasury indicators for 2010/11. 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).

Recent 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.

Member training on financial matters and treasury management issues was undertaken during the year on 18 May 2011 in order to support Members' scrutiny role.

During 2010/11, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

	2009/10 Actual £'000	2010/11 Estimate £'000	2010/11 Actual £'000
Actual capital expenditure	11,687	12,262	11,470
Total Capital Financing Requirement:			
• Non-HRA	-8	-5,261	-22
• HRA	-3,190	-2,570	-3,148
• Total	-3,198	-7,831	-3,170

Actual prudential and treasury indicators	2009/10	2010/11	2010/11
	Actual	Estimate	Actual
	£'000	£'000	£'000
Net borrowing requirement	0	0	0
External debt	2,000	2,000	2,000
Investments			
• Longer than 1 year	281	200	132
• Under 1 year	16,513	16,600	16,706
• Total	16,794	16,800	16,838

The difference in the 2010/11 Non-HRA Capital Financing Requirement between the Estimate and Actual is due to a change in accounting treatment of deferred grants which means that they are no longer taken into account when calculating the CFR. Other prudential and treasury indicators are to be found in the main body of this report.

The financial year 2010/11 continued the challenging environment of previous years; low investment returns and continuing counterparty risk continued.

The Council's Capital Expenditure during 2010/11 was funded without the need to borrow and as shown in the table above the council has a negative Capital Financing Requirement. The Council had one borrowing of £2m at the beginning and end of the year and no new borrowings were undertaken during 2010/11.

1. Treasury Position as at 31 March 2011

The Council's debt and investment position is organised by the treasury management section in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through Member reporting, as agreed by Council, and through officer activity detailed in the Council's Treasury Management Practices. At the beginning and the end of 2010/11 the Council's treasury position was as follows:

	31 March 2011	Rate/ Return	Average Life yrs	31 March 2010	Rate/ Return	Average Life yrs
TABLE I	Principal			Principal		
	£m	%		£m	%	
Fixed rate funding:						
-Market	2.0	11.625%	14	2.0	11.625%	15
Total debt	2.0	11.625%	14	2.0	11.625%	15
Investments:						
- in house	6.3	1.06%	-	3.6	0.58%	-
- with managers	10.5	1.22%	-	16.4	1.24%	-
Total investments	16.8	1.16%	-	20.0	1.02%	-

The maturity structure of the investment portfolio was in line with the Treasury Strategy as was the exposure to fixed and floating rate investments.

2. Performance Measurement

The target for both in-house and external investments is to be within 10 'basis points' of the 7 day LIBID rate for the year. LIBID is an inter bank rate commonly used for benchmarking such as this and for 2010/11 the average rate was 0.52% giving a spread of 0.42% to 0.62%. Both the internal and external managed funds comfortably exceeded this target.

Whilst both funds beat the benchmark we under achieved the budget figure of £320k by £50k with interest received from investing activities being £270k. Once again this was due to interest rates not rising as originally expected as well as a more limited range of institutions to invest with as a result of continued low credit ratings. In addition, £1.8m of capital receipts were used during the year to fund new capital expenditure in the borough.

3. The Strategy for 2010/11

The expectation for interest rates within the strategy for 2010/11 anticipated low but rising Bank Rate (starting in the fourth quarter of 2010) with similar gradual rises in medium and longer term fixed interest rates over 2010/11. Variable or short-term rates were expected to be the cheaper form of borrowing 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 low counterparty risk considerations, resulting in relatively low returns.

4. The Economy and Interest Rates

2010/11 proved to be another watershed year for financial markets. Rather than a focus on individual institutions, market fears moved to sovereign debt issues, particularly in the peripheral Euro zone countries. Local authorities were also presented with changed circumstances following the unexpected change of policy on Public Works Loan Board (PWLB) lending arrangements in October 2010. This resulted in an increase in new borrowing rates of 0.75 – 0.85%, without an associated increase in early redemption rates. This made new borrowing more expensive.

UK growth proved mixed over the year. The first half of the year saw the economy outperform expectations, although the economy slipped into negative territory in the final quarter of 2010 due to inclement weather conditions. The year finished with prospects for the UK economy being decidedly downbeat over the short to medium term while the Japanese disasters in March, and the Arab Spring, especially the crisis in Libya, caused an increase in world oil prices, which all combined to dampen international economic growth prospects.

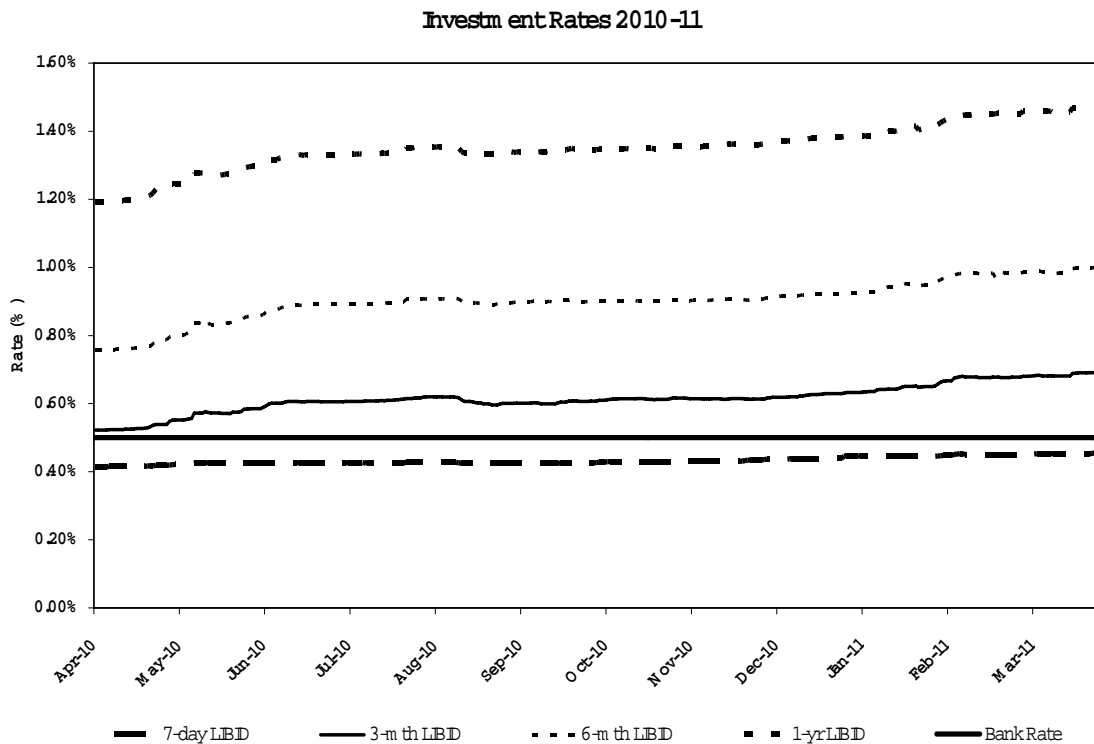
The change in the UK political background was a major factor behind weaker domestic growth expectations. The new coalition Government struck an aggressive fiscal policy stance, evidenced through heavy spending cuts announced in the October Comprehensive Spending Review, and the lack of any "giveaway" in the March 2011 Budget. Although the main aim was to reduce the national debt burden to a sustainable level, the measures are also expected to act as a significant drag on growth.

5. Investment Rates in 2010/11

The tight monetary conditions following the 2008 financial crisis continued through 2010/11 with little material movement in the shorter term deposit rates. Bank Rate remained at its historical low of 0.5% throughout the year, although growing market expectations of the imminence of the start of monetary tightening saw 6 and 12 month rates picking up.

Overlaying the relatively poor investment returns was the continued counterparty concerns, most evident in the Euro zone sovereign debt crisis which resulted in rescue packages for Greece, Ireland and latterly Portugal. Concerns extended to the European banking industry with an initial stress testing of banks failing to calm counterparty fears, resulting in a second round of testing currently in train. This highlighted the ongoing need for caution in treasury investment activity.

	Overnight	7 Day	1 Month	3 Month	6 Month	1 Year
01/04/2010	0.41%	0.41%	0.42%	0.52%	0.76%	1.19%
31/03/2011	0.44%	0.46%	0.50%	0.69%	1.00%	1.47%
High	0.44%	0.46%	0.50%	0.69%	1.00%	1.47%
Low	0.41%	0.41%	0.42%	0.52%	0.76%	1.19%
Average	0.43%	0.43%	0.45%	0.61%	0.90%	1.35%
Spread	0.03%	0.04%	0.07%	0.17%	0.24%	0.28%
High date	31/12/2010	30/03/2011	31/03/2011	31/03/2011	31/03/2011	31/03/2011
Low date	01/04/2010	01/04/2010	01/04/2010	01/04/2010	01/04/2010	01/04/2010



6. Investment Outturn for 2010/11

Investment Policy – the Council’s investment policy is governed by CLG guidance, which was implemented in the annual investment strategy approved by Council on 26 April 2010. 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.).

The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties. Investment performance by the fund managers, Investec Asset Management Ltd and the in-house management is shown in Table I above. Please note that the amounts shown are year end balances and the in-house managed funds do vary through the year and reflect the council’s cash flow during 2010/11.

Investments held by the Council - the Council maintained an average balance of £10.9m of internally managed funds. The internally managed funds earned an average rate of return of 1.06%. The comparable performance indicator is the average 7-day LIBID rate which was 0.52%.

7. Icelandic Bank Defaults

This authority had an investment of £1m, plus accrued interest, frozen in Heritable Bank Plc, a subsidiary of an Icelandic bank.

The Icelandic Government has stated its intention to honour all its commitments as a result of their banks being placed into receivership. The U.K. Government is working with the Icelandic Government to help bring this about. At the current time, the process of recovering assets is still ongoing with the administrators. The Local Government Association is co-ordinating the efforts of all UK authorities with Icelandic investments. Members will be periodically updated on the latest developments on these efforts.

As at 18 November 2011, the council has received £670k from the administrators and a further payment is expected in January 2012. The administrators are now predicting a return to investors of between 86p and 90p in the pound.

Lead Member

Cllr Tom Barkley

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Background Papers:

Cabinet report on Treasury Management Strategy Statement etc 17 March 2011

Appendix I: Prudential and treasury indicators

I. PRUDENTIAL INDICATORS	2009/10	2010/11	2010/11
Extract from budget and rent setting report	Actual	Forecast	Actual
	£'000	£'000	£'000
Capital Expenditure			
Non - HRA	£7,235	£7,346	£5,951
HRA	£4,452	£4,916	£5,519
TOTAL	£11,687	£12,262	£11,470
Ratio of financing costs to net revenue stream			
Non - HRA	-0.35%	-0.67%	-0.28%
HRA	2.25%	2.33%	6.03%
Net borrowing requirement			
brought forward 1 April	£0	£0	£0
carried forward 31 March	£0	£620	£0
in year borrowing requirement	£0	£620	£0
Capital Financing Requirement as at 31 March			
Non – HRA	-£8	-£5,261	-£22
HRA (applies only to housing authorities)	-£3,190	-£2,570	-£3,148
TOTAL	-£3,198	-£7,831	-£3,170
Annual change in Cap. Financing Requirement			
Non – HRA	£0	£0	£0
HRA (applies only to housing authorities)	£0	£620	£0
TOTAL	£0	£620	£0
Incremental impact of capital investment decisions	£ p	£ p	£ p
Increase in council tax (band D) per annum	-£0.20	£0.00	-£2.13
Increase in average housing rent per week (housing authorities only)	£0.00	£0.00	£0.00

2. TREASURY MANAGEMENT INDICATORS	2009/10	2010/11	2010/11
	Actual	Forecast	Actual
	£'000	£'000	£'000
Authorised Limit for external debt -			
borrowing	£8,000	£8,000	£8,000
other long term liabilities	£0	£0	£0
TOTAL	£8,000	£8,000	£8,000
Operational Boundary for external debt -			
borrowing	£5,000	£5,000	£5,000
other long term liabilities	£0	£0	£0
TOTAL	£5,000	£5,000	£5,000
Actual external debt	£2,000	£2,620	£2,000
Upper limit for fixed interest rate exposure			
Net principal re fixed rate borrowing / investments	100%	100%	100%
Upper limit for variable rate exposure			
Net principal re variable rate borrowing / investments	75%	75%	75%
Upper limit for total principal sums invested for over 364 days	50%	50%	50%