



Haringey Council
Agenda item:

General Purposes Committee

On 11 January 2011

Report Title.	Treasury Management 2010/11 Quarter 3 Activity & Performance update	
Report of:	Director of Corporate Resources	
Signed :		
Contact Officer :	Nicola Webb, Head of Finance: Treasury & Pensions Telephone 020 8489 3726	
Wards(s) affected: All	Report for: Non Key Decision	
1. Purpose of the report		
1.1.	To update the Committee on the Council's treasury management activities and performance in the third quarter of 2010/11.	
1.2.	To report to the Committee the results of the selection exercise undertaken to add further Money Market Funds to the lending list.	
2. Recommendations		
2.1	That members note the Treasury Management activity undertaken during the third quarter of 2010/11 and the performance achieved.	
2.2	That members approve the selection of the following additional Money Market Funds for the lending list:	
	<ul style="list-style-type: none">• J.P. Morgan Asset Management Sterling Liquidity Fund - £20m limit• Invesco Short Term Investments Company Sterling Liquidity Portfolio - £5m limit• BlackRock Institutional Sterling Liquidity Fund - £20m limit• BlackRock Institutional Government Sterling Liquidity Fund - £12m limit	

3. Reason for recommendations

- 3.1 To ensure members are aware of the Treasury Management activities undertaken in the third quarter of 2010/11 and to report on performance.
- 3.2 To provide further capacity for the Council's investments in line with the change to the Treasury Management Strategy Statement agreed on 18th October 2010 by Council and to provide the ability to diversify Money Market Fund deposits.

4. Summary

- 4.1 This report sets out the Council's Treasury Management activity and performance during the third quarter of 2010/11 and shows compliance against the Prudential Indicators and the Treasury Management Strategy Statement.
- 4.2 During the quarter, £40m of long term borrowing matured and was repaid to the PWLB. As a result, cash balances have reduced and so funds have been invested short term in money market funds and an instant access call account.
- 4.3 Officers and staff of the Council's Treasury Management Advisers, Arlingclose have interviewed the fund managers of four Money Market Funds and recommend that the funds offered by three of the companies are selected as additional funds for the lending list.

5. Head of Legal Services Comments

- 5.1 The Head of Legal Services has been consulted on the content of this report and comments that it's content and recommendations are within the policy agreed by Council and consistent with the purposes of Financial Regulations. In considering the report Members must take into account the expert financial advice available in the report and any further advice given at the meeting of the Committee in relation to the level of risk inherent in the proposals.

6. Use of appendices

- 6.1 Appendix 1: Summary of Treasury Management Activity and Performance
Appendix 2: Prudential Indicators

7. Local Government (Access to Information) Act 1985

7.1 The following background papers were used in the preparation of this report:

- Financial Planning Report for 2010/11 to 2011/13 reported to Council and agreed on 22nd February 2010.
- Treasury Management reports to General Purposes Committee 28th June 2010 and 23rd September 2010.

For access to the background papers or any further information please contact Nicola Webb, Head of Finance: Treasury & Pensions, on 0208 489 3726.

8. Treasury Management Strategy Statement 2010/11

8.1 The Council approved the Treasury Management Strategy Statement for 2010/11 on 22nd February 2010. The Strategy states that General Purposes Committee will monitor treasury management activity and performance on a quarterly basis. This report forms the third quarterly monitoring report for 2010/11.

8.2 The government guidance on local authority treasury management states that local authorities should consider the following factors in the order they are stated:

Security - Liquidity - Yield

The Treasury Management Strategy reflects these factors and is explicit that the priority for the Council is the security of its funds.

8.3 The quarterly reports during 2010/11 are structured according to these factors, so that members can see how they are being addressed operationally.

9. Treasury Management Activity and Performance: Security

9.1 The Treasury Management Strategy Statement places a high emphasis on security of the Council's funds. This is achieved in two ways; firstly by minimising the funds held which need to be invested; and, secondly by maintaining a lending list of high quality counterparties with strict limits.

9.2 During the financial year to date cash balances have remained at levels sufficient to manage the payments the Council was required to make. £40m of PWLB long term borrowing matured in October bringing the total maturities this year to £50m. So far this financial year new borrowing of £20m has been taken and the remainder has

been funded through the use of cash balances. The long term borrowing portfolio now totals £606m and the average rate payable has dropped to 6.71%.

- 9.3 As part of the Spending Review in October, the interest rates payable on borrowing from the PWLB have been increased to 1% above the government's cost of borrowing. This was done with immediate effect for all new borrowing. The Council's existing borrowing is unaffected by this.
- 9.4 The Council approved the list of institutions which the Council can lend to as part of the Treasury Management Strategy Statement. The list was drawn up on the advice of the Council's treasury management advisers and only includes institutions which are assessed as having high credit quality. As the cash balances have reduced during the quarter following the repayment of £40m PWLB borrowing, it has been necessary to invest cash on a short term basis only for liquidity reasons.
- 9.5 Three AAA rated money market funds were selected for use by the Council following a selection exercise in November 2009. These funds have been used extensively due to the instant access they offer and a rate of return comparable to that achievable for a one month fixed term deposit. In addition the instant access account offered by Santander UK has been used since the agreement to reinstate it onto the lending list in September.
- 9.6 The Council has sought to minimise its security risk by setting limits on each institution on the lending list. The Council has complied with all these limits during the financial year to date. In addition officers have sought to spread the deposits across the available institutions to further minimise security risk. The table below shows the Council's deposits on 22nd December 2010:

Institution	Long Term Credit Rating	Amount (£m)	% of total deposits
Henderson Money Market Fund	AAA	11.70	37
RBS Money Market Fund	AAA	6.02	19
Santander UK	AA-	14.00	44
Total		31.72	100

- 9.7 Arlingclose, the Council's treasury management advisers, have devised a way of scoring the level of credit risk the Council is taking. The scores this produces have been reported to General Purposes Committee since early 2009/10. This measure scores credit risk on a scale of 0 to 10 on both a value weighted and a time weighted basis and the table below demonstrates how to interpret the scores:

Above target	AAA to AA+	Score 0 - 2
Target score	AA to A+	Score 3 - 5
Below target	Below A+	Score over 5

- 9.8 The score for the latest quarter is shown below alongside the previous three quarters for comparison:

	Quarter 4 2009/10	Quarter 1 2010/11	Quarter 2 2010/11	Quarter 3 2010/11
Value weighted	3.5	2.3	2.7	2.2
Time weighted	4.2	3.6	4.2	1.9

The scores are lower than those in the previous quarter due to the significant use of money market funds which attract a low score as they have the highest rating (AAA) and are instant access.

10. Treasury Management Activity and Performance: Liquidity

- 10.1 Once the Council is satisfied that security risk is being managed, the next consideration in treasury management is liquidity. The Council has a number of inflows and outflows every month and it is important that the Council's funds are managed to ensure there is sufficient liquidity when it is required.
- 10.2 The tool which officers use to ensure that liquidity is maintained is cash flow forecasting. Work has been done to develop the forecasting and officers now have a clearer picture of day to day liquidity requirements.
- 10.3 Officers have maintained liquidity throughout the quarter. As discussed above, the cash balances have reduced in the quarter and so liquidity has been maintained through extensive use of AAA rated money market funds and the instant access account with Santander UK. These investments offer instant access for a rate of return comparable to that achievable on a one month fixed term deposit.
- 10.4 The table below shows the Council's deposits at 22nd December 2010, the term of each of the deposits and calculates the weighted average maturity of the portfolio. Due to the sole use of instant access investments at present, the weighted average maturity at present is one day.

Institution	Term of deposit (days)	Amount (£m)
Henderson Money Market Fund	1	11.70
RBS Money Market Fund	1	6.02
Santander UK	1	14.00
Weighted Average Maturity	1	31.72

11. Treasury Management Activity and Performance: Yield

- 11.1 Only once security and liquidity have been considered and the Council is satisfied it has taken all steps to minimise these risks, should yield be a factor. Base rate has remained at 0.5% throughout the financial year to date and Arlingclose's forecast is that it will remain at this rate until at least the end of 2011 when it will start to rise slowly.
- 11.2 The money market funds are paying between 0.5% and 0.6% and Santander UK is currently paying 0.8% on the instant access call account.
- 11.3 By the end of the third quarter of the financial year, it is expected that interest of £212k will have been earned on the Council's deposits at an average rate of 0.6%. The interest payable on borrowing by the end of the third quarter was £32.4m. The budget for interest earned in 2010/11 is £500k and the budget for interest payable is £44.57m. An underspend of £2m is projected by the end of the financial year, which is as a result of reducing cash balances instead of taking on additional external borrowing to refinance the maturing loans and fund capital expenditure.

12. Prudential Indicators

- 12.1 The Council set prudential indicators for 2010/11 in February 2010. The set of indicators is made up of those which provided an indication of the likely impact of the planned capital programme and those which are limits set on treasury management activity. Appendix 2 sets out the original indicators, the current forecast for each of the capital indicators and the current position on each of the treasury management limits.
- 12.2 Forecast capital expenditure has increased since the original indicator was set due to the addition of carry forwards from 2009/10. The incremental impact of capital expenditure indicators are showing much lower levels than originally set. The original indicators showed the total Band D Council Tax and weekly housing rent, rather than only the portion related to capital expenditure not supported by grants.
- 12.3 None of the limits on treasury management have been breached in the year to date. Borrowing is significantly lower than was anticipated when the limits were set, due to the policy of using internal cash balances to fund the capital programme. Long term liabilities have increased compared to the figures set in February 2010, due to the accounting changes brought about by the introduction of International Financial Reporting Standards. The total of borrowing and long term liabilities still remains well within the operational boundary and authorised limit.

13. Additional Money Market Funds

- 13.1 At the General Purposes Committee meeting on 23rd September 2010, it was recommended that the limits for money market funds be increased to £20m per Fund and the group limit increased to £100m. This was approved by full Council on 18th October 2010. It was agreed that the addition of any new Funds be subject to a selection exercise involving officers and the Council's treasury management advisers, Arlingclose Ltd.
- 13.2 On 26th November 2010 interviews took place with the fund managers of four Money Market Funds recommended by the Council's treasury management advisers. The Lead Finance Officer and Head of Finance: Treasury & Pensions were supported by Arlingclose staff in these interviews. The fund managers were questioned on a range of issues including investment strategy, the security of the investments, size of the fund, liquidity, yield and administrative processes. The key focus however was the security of the investments.
- 13.3 Following the interviews, officers and Arlingclose staff awarded the funds scores in the categories of security, size, liquidity and yield, with security being heavily weighted. The results of the scores are shown below:

	JP Morgan	Invesco	BlackRock	Ignis
Security	56.25	51.75	48.75	38.25
Size	34.5	22.0	36.5	23.5
Liquidity	19.0	19.0	19.0	11.5
Yield	11.5	14.0	15.5	19.0
TOTAL	121.25	106.75	119.75	92.25
Percentage score	86.6%	76.3%	85.5%	65.9%

- 13.4 It is clear from this that JP Morgan and BlackRock scored highly and therefore it is recommended that both these funds are added to the lending list with a £20m limit each. The reason Invesco's score was lower was the size of the fund. Arlingclose recommend that any investment the Council makes with a money market fund should be no more than 0.5% of the value of the total fund. Following a discussion with Arlingclose it is recommended that the Invesco fund is added to the list but with a lower limit of £5m reflecting the smaller size of the fund.
- 13.5 In addition to the main BlackRock money market fund, BlackRock also have a fund which invests in government securities only. It is recommended that this fund is also added to the lending list, because although the yield is significantly lower than other funds, it would be an appropriate fund in which to invest in the event of significant stress in the market, due to the government guarantee associated with the investments within the Fund. Due to the size of the fund, it is recommended that the limit is £12m.

14. Icelandic bank deposits update

- 14.1 The processes to recover the £36.957m deposited with Icelandic banks is continuing in conjunction with other local authorities.
- 14.2 The administration process for Heritable Bank is being undertaken by Ernst and Young in the UK. Their work is directed by the creditors' committee of which the Council is a member. 45% of Heritable deposits have now been returned – this amounts to £9m in the case of the Council and a further distribution is expected in January. The overall expected recovery rate is 80-85%.
- 14.3 Work to recover the deposits in Landsbanki and Glitnir is continuing through the Icelandic courts. The scale of recovery continues to hinge on whether the courts accept that the local authority deposits have priority. It is likely the appeals against the initial decisions that the Landsbanki are priority and the Glitnir ones are not, will be heard during 2011. The lawyers appointed on behalf of all local authorities are preparing the necessary cases and the Council is providing all the information it has about the deposits.

15. Recommendation

- 15.1 That members note the Treasury Management activity undertaken during the third quarter of 2010/11 and the performance achieved.
- 15.2 That members approve the selection of the following additional Money Market Funds for the lending list:
- J.P. Morgan Asset Management Sterling Liquidity Fund - £20m limit
 - Invesco Short Term Investments Company Sterling Liquidity Portfolio - £5m limit
 - BlackRock Institutional Sterling Liquidity Fund - £20m limit
 - BlackRock Institutional Government Sterling Liquidity Fund - £12m limit

Appendix 1: Summary of Treasury Management Activity and Performance

1. Treasury Portfolio

	Position at Q3 2010/11 £000	Position at Q2 2010/11 £000	Position at Q1 2010/11 £000
Long Term Borrowing PWLB	480,806	520,806	510,811
Long Term Borrowing Market	125,005	125,005	125,005
Short Term Borrowing	0	0	0
Total Borrowing	605,811	645,811	635,816
Investments: Council	31,720	67,770	87,934
Investments: Icelandic deposits in default	27,928	28,788	30,030
Total Investments	59,648	96,558	117,964
Net Borrowing position	546,163	549,253	517,852

2. Security measure

	Quarter 3 2010/11	Quarter 2 2010/11	Quarter 1 2010/11
Credit score – Value weighted	2.2	2.7	2.3
Credit score – Time weighted	1.9	4.2	3.6

3. Liquidity measure

	Quarter 3 2010/11	Quarter 2 2010/11	Quarter 1 2010/11
Weighted average maturity: deposits (days)	1.0	13.8	41.3
Weighted average maturity: borrowing (years)	23.8	22.6	21.6

4. Yield measure

	Quarter 3 2010/11	Quarter 2 2010/11	Quarter 1 2010/11
Interest rate earned	0.63%	0.54%	0.66%
Interest rate payable	6.71%	6.78%	7.00%

Appendix 2: Prudential Indicators

No.	Prudential Indicator	2010/11 Original Indicator		2010/11 Position/Forecast at Quarter 3
CAPITAL INDICATORS				
1	Capital Expenditure	£148,598k		£155,375k
2	Ratio of financing costs to net revenue stream			
	General Fund	4.67%		5.50%
	HRA	33.39%		31.42%
3	Capital Financing Requirement	£718,766k		£769,210k
4	Incremental impact of capital investment decisions			
	Band D Council Tax	£1,184.32		£9.96
	Weekly Housing rents	£83.20		£0.01
TREASURY MANAGEMENT LIMITS				
5	Authorised Limit	£900,000k		£658,813k
	Operational Boundary	£875,000k		£658,813k
6	Upper limit – fixed rate exposure	100%		98.5%
	Upper limit – variable rate exposure	40%		1.5%
7	Maturity structure of borrowing (U: upper, L: lower)	L	U	
	under 12 months	0%	25%	5.28%
	12 months and within 2 years	0%	25%	9.33%
	2 years and within 5 years	0%	50%	13.22%
	5 years and within 10 years	0%	75%	19.00%
	Over 10 years	0%	100%	53.17%
8	Sums invested for more than 364 days	£60,000k		£0
9	Adoption of CIPFA Treasury Management Code of Practice			√