Haringey Council

Report for:	Corporate Committee 28th June 2012	Item number	

Title:	Treasury Management 2011/12 Outturn & Quarter 1 2012/13 update

Report authorised by :	Interim Chief Financial Officer

Lead Officer:	Nicola Webb, Head of Finance – Treasury & Pensions nicola.webb@haringey.gov.uk 020 8489 3726

Ward(s) affected: N/A	**Report for** Non Key Decision

1. Describe the issue under consideration

1.1 This is a report to members on treasury management activity and performance during 2011/12 in accordance with the CIPFA Treasury Management Code of Practice. It is a requirement of the Code for this to be reported on to Council once Corporate Committee has considered it. In addition it provides an update for members on treasury management activity during the first quarter of 2012/13.

2. Cabinet Member Introduction

2.1 Not applicable.

3. Recommendations

3.1 That Members note the Treasury Management activity and performance during 2011/12 and the first quarter of 2012/13.

4. Other options considered

4.1 None.

5. Background information

5.1 The Council approved the Treasury Management Strategy Statement for 2011/12 on 24th February 2011. Corporate Committee is responsible for monitoring treasury management activity during the year and this was achieved through the receipt of quarterly reports. This outturn report is a requirement of the CIPFA Treasury Management Code of Practice and it summarises the activity during 2011/12.

5.2 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.

5.3 Prudential Indicators for 2011/12 were set by Council on 24th February 2011 and two were revised on 21st November 2011. They have been monitored on a quarterly basis during the year.

6. Comments of the Chief Financial Officer and Financial Implications

6.1 The treasury management strategy in 2011/12 was to continue to maximise internal borrowing and, therefore, to minimise cash balances. This policy not only reduced credit risk in the year but also reduced the cost of borrowing. In addition the policy of taking short term borrowing from other local authorities instead of long term also saved interest costs during 2011/12. As reported to June Cabinet in the Council's outturn report, the net underspend on the interest budget in 2011/12 as a result of these active management decisions was £1.389m.

7. Head of Legal Services and Legal Implications

7.1 The Head of Legal Services has been consulted on the content of this report. Its content and recommendation are in accordance the Treasury Management Strategy Statement and consistent with legislation governing the financial affairs of the Council.

8. Equalities and Community Cohesion Comments

8.1 There are no equalities issues arising from this report.

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9. Head of Procurement Comments

9.1 Not applicable.

10. Policy Implications

10.1 None applicable.

11. Use of Appendices

11.1 Appendix 1: Summary of Treasury Management activity & performance
Appendix 2: Prudential Indicators

12. Local Government (Access to Information) Act 1985

12.1 Not applicable.

13. Economic and treasury portfolio background in 2011/12

13.1 The UK Bank Rate remained at 0.5% throughout the financial year as the UK economy struggled and then entered recession in the latter part of the year. Issues in the Eurozone continued to dominate markets throughout the year and the concerns around bank exposures to the weaker economies led to a number of credit rating downgrades for banks, as well as the countries themselves. This background meant short term investment rates remained only marginally above 0.5% during 2011/12.

13.2 The Localism Act passed into law in November 2011 which enabled the reform of council housing finance. The Housing Revenue Account subsidy system has now been abolished and replaced with self-financing whereby authorities support their own housing stock from their own income. This reform required a readjustment of each authority's housing-related debt based on a valuation of its council housing stock. For the Council this meant that on 28th March 2012, £233.85m of outstanding PWLB loans were repaid by the Department for Communities and Local Government.

13.3 The position of the treasury portfolio at the end of the financial year compared to the previous financial year end is shown in the table below. This shows the reduction in PWLB borrowing resulting from the repayment of debt in respect of housing reform and a reduction in the cash balances invested. The sections which follow describe the activity in the borrowing and investment portfolios.

Treasury Portfolio	Position at 31/03/11 £000	Position at 31/03/12 £000
Borrowing		
PWLB Fixed Maturity	460,806	201,544
PWLB Fixed EIP	24,000	9,682
PWLB Variable EIP	18,000	7,746
Market loans	125,000	125,000
Other Local authorities	3,000	50,000
Total External Borrowing	630,806	393,972
Investments		
Fixed Term Deposits	3,400	0
Call Accounts	10,400	0
Money Market Funds	14,235	5,470
Total Investments	28,035	5,470

14. Long Term Borrowing

14.1 In 2010/11 the Council undertook little external borrowing as it moved towards maximising the use of internal balances in lieu of borrowing. The reason for this was to minimise the "cost of carry" associated with external borrowing. The cost of carry is the difference between the interest rate paid for long term borrowing, and the rate of interest which can be earned from temporarily investing the funds borrowed. This has amounted to 3.5-4% in the last couple of years. In 2011/12 this policy continued, although there was a finite limit to the amount of "internal borrowing" which could be done and so £50m of the £53m of maturing loans was required to be refinanced.

14.2 On 28th March 2012 £233.85m of PWLB debt was repaid by the Department of Communities & Local Government as part of housing reform. It was announced early in the financial year that the repayment would be done by repaying a proportion of every loan the Council had outstanding. Therefore in order to maximise the amount of higher rate loans repaid, the refinancing was achieved by borrowing for periods of 1 year or less from other local authorities. Undertaking short term borrowing from local authorities at an average rate of 0.83% also ensured lower than anticipated expenditure on interest payments.

14.3 The table below summarises the transactions undertaken during the financial year:

	01/4/11 £000	Maturing loans £000	Repay-ments re HRA £000	New loans £000	31/3/12 £000
PWLB Fixed Maturity	460,806	(44,500)	(214,762)	0	201,544
PWLB Fixed EIP	24,000	(4,000)	(10,318)	0	9,682
PWLB Variable EIP	18,000	(1,484)	(8,770)	0	7,746
Market loans	125,000	0	0	0	125,000
Other Local Authority	3,000	(3,000)	0	50,000	50,000
Total borrowing	630,806	(52,984)	(233,850)	50,000	393,972

14.4 At the end of the financial year the average interest payable on the borrowing portfolio had fallen to 5.87% from 6.8% at 1st April 2011.

15. Investments – activity and performance in 2011/12

15.1 The Council held average cash balances of £41.6m during the year. The balances represented working cash balances and the Council's reserves. The Council invested these funds in accordance with the Treasury Management Strategy Statement agreed for 2011/12. All investments made during the year complied with the Council's agreed Treasury Management Strategy, Prudential Indicators, Treasury Management Practices and prescribed limits. Maturing investments were repaid to the Council in full and in a timely manner.

15.2 The Council's investment priorities set out in the 2011/12 strategy were:
1) Security of the invested capital;
2) Liquidity of the invested capital;
3) An optimum yield which is commensurate with security and liquidity.
The investments placed by the Council during 2011/12 reflected these priorities.

15.3 Counterparty credit quality was assessed and monitored with reference to credit ratings (the Council's minimum long term counterparty rating of A+ across all three rating agencies – Fitch, Standard & Poors and Moody's); credit default swaps; any potential support mechanisms from the UK government and share price. 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 2011/12.

15.4 In October 2011, many UK banks were downgraded to a level below the minimum level acceptable for the Council's lending list. In anticipation of this happening, the Council had only been investing in UK banks on an instant access basis for some time prior to the announcement. All monies which were invested with these banks were withdrawn immediately in full. The result of the downgrades was that the Council only invested in instant access AAA rated Money Market Funds and the government guaranteed Debt Management Office for much of the second half of the financial year. The table below shows the investments outstanding on 31st March 2012:

Institution	Long Term Credit Rating	Amount (£m)	% of total deposits
BlackRock MMF	AAA	0.905	16.5
Deutsche MMF	AAA	0.220	4.0
Goldman Sachs MMF	AAA	0.400	7.3
Invesco MMF	AAA	2.200	40.2
JP Morgan MMF	AAA	0.375	6.9
RBS MMF	AAA	1.370	25.1
Total		5.470	100.0

15.5 Throughout 2011/12 credit risk scores have been reported to Corporate Committee, based on a methodology devised by Arlingclose, the Council's treasury management advisers. The scores show 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

15.6 The scores during 2011/12 are shown overleaf and show the impact of moving to investing only in AAA rated money market funds and the Debt Management Office:

	Quarter 1 2011/12	Quarter 2 2011/12	Quarter 3 2011/12	Quarter 4 2011/12
Value weighted	2.6	2.5	1.0	1.0
Time weighted	1.8	1.8	1.0	1.0

15.7 Liquidity has been maintained throughout the year through the extensive use of AAA rated money market funds, which operate on an instant access basis. As all of the Council's funds were invested in money market funds on 31st March 2012, the weighted average maturity of the investment portfolio was 1 day.

15.8 £251k of interest was earned on the Council's investments during 2011/12 at an average rate of 0.60%, 0.10% above the Bank of England base rate.

16. Update on Icelandic deposits

16.1 In April 2011 the Icelandic District Court decided that local authority deposits in Landsbanki and Glitnir had priority status. The decision was subsequently upheld by the Icelandic Supreme Court following an appeal in October 2011. This means the expected recovery rates are now 100% for Glitnir and 98% for Landsbanki. Following these announcements the first distributions from Glitnir and Landsbanki were received. At the time of writing a total of £7.23m had been received in respect of Glitnir and Landsbanki.

16.2 In addition to the distributions received, monies totalling around £1m have been distributed in Icelandic krona. However due to exchange rate controls, this cannot be removed from Iceland. It is therefore being held in escrow and the legal advisers working on behalf of all local authorities are liaising with Iceland and UK government officials to investigate ways of getting the monies released.

16.3 The administrators of Heritable Bank continued to make distributions during the year and their current base case is a recovery rate of 86-90% of the amounts originally invested.

16.4 In total £21.5m has been returned to the Council to date which makes up 58% of the total amount originally invested of £36.9m.

17. Compliance with Prudential Code indicators

17.1 The Council set prudential indicators for 2011/12 in February 2011. 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. Updates to two of the indicators were agreed by Council in November 2011. Appendix 2 sets out the approved indicators for 2011/12 and the final position for each of the capital indicators and the year end position on each of the treasury management limits.

17.2 None of the limits on treasury management have been breached in the year to date. Borrowing is well within the operational and authorised limits, as the peak of borrowing was £657.8m in September 2011. The continued policy of using internal cash balances to fund the capital programme ensured this was the case. The repayment of HRA borrowing on 28th March 2012 has resulted in some of the figures looking significantly lower than forecast, however it has been necessary to have limits at the higher level to ensure there were no breaches in the period up to 28th March 2012.

17.3 The budget outturn report to Cabinet on 12th June 2012 set out the capital expenditure in 2011/12 and reasons for the movement from the original indicator. The capital expenditure figure in this report includes £4.28m capitalisation for redundancy costs. The impact on Council Tax indicator measures the impact on Band D council tax of the costs of borrowing to fund the capital programme. The capitalisation of redundancy costs is classed as borrowing as it will be funded over the long term. This was not taken into account at the time the original council tax impact indicator was set, as the capitalisation had not been agreed by central government. This is the reason this indicator has increased so much since the original one was set.

18. 2012/13 quarter 1 update

18.1 During the quarter £20m of local authority borrowing has matured, however due to the pattern of the Council's cashflow where more money comes in early in the financial year, it has only been necessary to refinance £5m. This was borrowed again from Derbyshire County Council at 0.70%, a lower rate than previously.

18.2 Moodys rating agency placed all UK banks on review for possible downgrade in February 2012 with a view to announcing the results of the review in May or June 2012. At the time of writing, the result of the review has not been announced, but there remains a significant risk that some or all of the banks on the Council's lending list are downgraded below the minimum criteria agreed in the Treasury Management Strategy. For this reason the Council has been investing in UK banks on an instant access basis only. Extensive use continues to be made of AAA rated instant access money market funds and the Debt Management Office.

18.3 The table below shows the Council's investments as at 11th June 2012. At this point in time balances are relatively high pending large payments and loan maturities expected later in the month.

Counterparty	Long Term Credit Rating	Period to maturity	Amount (£k)	% of total deposits
Debt Management Office	AAA*	2	5,050	15.0%
Debt Management Office	AAA*	9	3,700	11.0%
Debt Management Office	AAA*	9	5,900	17.5%
Debt Management Office	AAA*	11	3,150	9.3%
Nat West Call Account	A	1	6,700	19.9%
BlackRock Money Market Fund	AAA	1	1,800	5.3%
Deutsche Money Market Fund	AAA	1	1,700	5.1%
Goldman Sachs Money Market Fund	AAA	1	2,000	5.9%
JP Morgan Money Market Fund	AAA	1	2,000	5.9%
RBS Money Market Fund	AAA	1	1,700	5.1%
Total			33,700	

* The Debt Management Office does not have a credit rating, therefore the UK sovereign rating is shown.

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Appendix 1: Summary of Treasury Management Activity & Performance

1. Treasury Portfolio

	Position at Q4 2011/12 £000	Position at Q3 2011/12 £000	Position at Q2 2011/12 £000	Position at Q1 2011/12 £000
Long Term Borrowing PWLB	218,972	469,806	490,806	502,806
Long Term Borrowing Market	125,000	125,000	125,000	125,000
Short Term Borrowing	50,000	43,000	13,000	3,000
Total Borrowing	393,972	637,806	628,806	630,806
Investments: Council	5,470	40,849	29,110	49,140
Investments: Icelandic deposits in default	19,441	24,107	24,939	25,746
Total Investments	24,911	64,956	54,049	74,886
Net Borrowing position	369,061	572,850	574,757	555,920

2. Security measure

	Quarter 4 2011/12	Quarter 3 2011/12	Quarter 2 2011/12	Quarter 1 2011/12
Credit score – Value weighted	1.0	1.0	2.5	2.6
Credit score – Time weighted	1.0	1.0	1.8	1.8

3. Liquidity measure

	Quarter 4 2011/12	Quarter 3 2011/12	Quarter 2 2011/12	Quarter 1 2011/12
Weighted average maturity: deposits (days)	1	3.95	1	1
Weighted average maturity: borrowing (years)	24.80	21.83	22.18	22.35

4. Yield measure

	Quarter 4 2011/12	Quarter 3 2011/12	Quarter 2 2011/12	Quarter 1 2011/12
Interest rate earned	0.39%	0.67%	0.77%	0.70%
Interest rate payable	5.87%	6.05%	6.43%	6.49%

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Appendix 2: Prudential Indicators

No.	Prudential Indicator	2011/12 Approved Indicator		2011/12 Position/Actual at 31/03/12
CAPITAL INDICATORS				
1	Capital Expenditure	£79,874k		£89,340k
2	Ratio of financing costs to net revenue stream			
	General Fund	4.95%		4.49%
	HRA	31.90%		26.65%
3	Capital Financing Requirement	£773,366k		£495,617k
4	Incremental impact of capital investment decisions			
	Band D Council Tax	£1.00		£2.91
	Weekly Housing rents	£0.02		£0.01
TREASURY MANAGEMENT LIMITS				
5	Authorised Limit	£946,879k		£393,972k
	Operational Boundary	£818,434k		£393,972k
6	Upper limit – fixed rate exposure	100%		95.85%
	Upper limit – variable rate exposure	40%		4.15%
7	Maturity structure of borrowing (U: upper, L: lower)	L	U	
	under 12 months	0%	25%	17.98%
	12 months & within 2 years	0%	25%	6.23%
	2 years & within 5 years	0%	50%	9.64%
	5 years & within 10 years	0%	60%	10.21%
	10 yrs & within 20 yrs	0%	60%	5.54%
	20 yrs & within 30 yrs	0%	60%	3.07%
	30 yrs & within 40 yrs	0%	60%	2.54%
	40 yrs & within 50 yrs	0%	60%	25.76%
	50 yrs & above	0%	60%	19.03%
8	Sums invested for more than 364 days	£20,000k		£0
9	Adoption of CIPFA Treasury Management Code of Practice	√		√