

This report ensures the council is embracing best practice in accordance with CIPFA's recommendations, by keeping members informed of Treasury Management activity.

1. The Economy

1.1. Recent economic statistics show the following:

- The Bank Base Rate remaining unchanged at 0.50%.
- Inflation remaining well above target. In April Consumer Price Inflation rose from 4.0% to 4.5% and remained at 4.5% in May. Gas and electricity hikes could push inflation close to 5% in 2011.
- The UK economy growing but only modestly. The outlook for exports remains positive but domestic retail sales are contracting due to a fall in disposable income, weak house price growth and a lack of consumer confidence.
- The higher inflation projection and weaker outlook for growth increases the dilemma for the Bank of England regarding any movement in Base Rate
- Unemployment is just under 2.5 million and will increase as the public sector shrinks but private sector employment grows at only a modest pace.

2. The Council's Investments

2.1 As at 31 May 2011 the council held the following investments:

Investment	Term	Maturity Date	Interest Rate	Amount invested £m	£m
Instant access bank accounts:					
National Westminster	N/A	N/A	1.10%	5.00	
Royal Bank of Scotland	N/A	N/A	1.10%	2.50	
Santander	N/A	N/A	0.80%	5.00	12.50
Instant access Money Market Funds:					
Prime Rate	N/A	N/A	0.73%	5.00	
Ignis	N/A	N/A	0.74%	5.00	
Standard Life	N/A	N/A	0.65%	0.77	10.77
Rolling monthly programme of £1 million one year term deposits:					
Lloyds	364 days	27/07/11	1.95%	1.00	
Lloyds	364 days	19/08/11	1.95%	1.00	
Barclays	364 days	16/09/11	1.46%	1.00	
Nationwide	334 days	25/10/11	1.25%	1.00	
Nationwide	364 days	24/11/11	1.33%	1.00	
Bank of Scotland	335 days	28/12/11	1.82%	1.00	
Bank of Scotland	364 days	26/01/12	1.95%	1.00	
Bank of Scotland	364 days	13/02/12	2.05%	1.00	
Newcastle City Council	364 days	15/03/12	1.55%	1.00	
Bank of Scotland	364 days	05/04/12	2.05%	1.00	
Bank of Scotland	364 days	02/05/12	2.05%	1.00	11.00
Other fixed term deposits:					
Nationwide	215 days	05/12/11	1.09%	1.00	
Nationwide	245 days	01/01/12	1.14%	1.00	
Barclays	275 days	27/01/12	1.32%	1.00	

Nationwide	278 days	06/02/12	1.19%	1.00	
Newcastle City Council	339 days	27/02/12	1.48%	2.00	
Barclays	306 days	27/02/12	1.41%	1.00	
Barclays	328 days	20/03/12	1.47%	1.00	
Lloyds TSB	449 days	27/07/12	2.65%	0.50	8.50
Total					42.77

The term deposits shaded grey are those placed in the last two months

- 2.2 At the time of writing, the council has completed its rolling programme of one year £1 million deposits. Subject to funds being available, each month the council will renew the maturing deposit after careful consideration of the opportunities available.
- 2.3 Following a fall in the short-term interest rates being charged by the Public Works Loan Board, the rate being paid by other local authorities has also fallen. Currently the council could only obtain 1.10% for a one year deposit with another Local Authority so deposits placed earlier in the year with Newcastle City Council have proved beneficial.
- 2.4 The political and economic crisis in Greece has led Arlingclose to revise its recommended maximum maturity limits (both foreign and UK institutions) from two years to one year. Arlingclose has investigated the implications of a Greek default and although the implications are serious they do not believe that it would lead to widespread contagion. Research into bank exposure to Greek debt identifies that, after the Greek banks, the largest exposure rests with the French banks followed by German banks. UK banks are exposed to a total of just over £2 billion of Greek debt. To put this in perspective UK banks have recently and collectively made provisions of £5.45 billion for the mis-selling of payment protection insurance.
- 2.5 Because of the uncertainty in Europe, the council will continue restricting its investments to the largest of the UK institutions.
- 2.6 On 5th May 2011 Lloyds/Bank of Scotland Group launched a new term deposit offering 2.65% for the period to 27th July 2012. The council invested £500,000, which was the remaining amount within the counterparty limit. This is the only term deposit that the council has made for a period exceeding one year.
- 2.7 To date there has been no change in the bank base rate and Arlingclose has provided the following forecast of the bank base rate (forecast provided in June 2011):

Bank Rate	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13
Upside risk	+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	0.50	0.75	1.00	1.25	1.50	1.75	2.00	2.25	2.50	2.75
Downside risk		-0.25	-0.25	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50

The forecast has changed since the February report with rates staying lower for longer. Arlingclose have put back the first increase in the Bank Base Rate from the third quarter in 2011 to the last quarter of the year.

- 2.8 The council has earned interest on its investments as follows:

Month	Average Invested £m	Average rate of interest earned	Amount of interest earned
April 2011	40.6	1.08%	£36,046
May 2011	47.4	1.15%	£46,099
Total			£82,145

2.9 With no change in the Base Rate on the horizon, the 2011/12 budget was set in January 2011 at the same level as in the previous year (£249,070). This budget is attainable and should result in a surplus for the year.

3. The Council's Borrowing

3.1 All short-term borrowing taken out towards the end of 2010/11 has now been repaid, the last loan being repaid on 4th May 2011.

3.2 The long-term borrowing budget was set in January 2011 at a time when PWLB rates were steadily increasing and there was concern over the interest rates that would need to be paid on future borrowing. Arlingclose's forecast was for the 20 year PWLB rate to reach 6% in the third quarter of 2011. In order to set a prudent budget, and give the council flexibility with regard to maturity periods, the budget was set using an interest rate of 5.75%. The borrowing budget can be analysed as follows:

	Budget	Forecast	Surplus
	£m	£m	£m
Minimum Revenue Provision	9.87	9.69	0.18
Interest on existing loans (January 2011 position)	5.43	5.43	-
Borrowing of £5m to be taken out before the end of 2010/11 (Budget 4.00%; Actual 3.71%)	0.20	0.18	0.02
Borrowing requirement for 2011/12 (£7m in budget; Forecast per capital programme £8m)	0.40	0.35	0.05
Borrowing of £10m to externalise internal borrowing used to support the capital programme in 2008/09 and 2009/10	0.58	0.43	0.15
Provision for refinancing of LOBO loans at a higher rate	0.12	0.07	0.05
Total	16.60	16.15	0.45

3.3 In fact PWLB interest rates reached a peak in mid-February and then there followed a month or two when rates were more volatile. Since mid-April rates have actually fallen back and today stand at around their November 2010 levels.

3.4 When interest rates were increasing rapidly it was a possibility that the council would borrow sooner rather than later. However the slowdown in the upward trend, then subsequent reversal, has meant that the council has yet to take out any new borrowing in 2011/12. The surplus shown above reflects this postponement and the resultant savings in interest charges. The surplus shown above does not at present incorporate savings due to lower interest rates which will be recognised as and when loans are taken out.