

This report ensures the council demonstrates best practice in accordance with CIPFA's recommendations in Code of Practice for Treasury Management, by keeping members informed of treasury management activity.

1. The Economy

1.1. Recent economic events and statistics show the following:

- The final estimate of economic growth for the third quarter showed the economy growing by 0.90% over the quarter and by 0% year on year. There are concerns over the result being influenced by one-off factors such as the Olympics and growth is not expected to be sustained.
- The Consumer Price Index (CPI) was 2.70% for both October and November. Its decrease towards the 2% target is anticipated to be slower than previously estimated due to volatility in commodity prices.
- Members of the Monetary Policy Committee voted unanimously to hold the Bank Rate at 0.50% at their meeting in December.
- The Eurozone is making slow headway, which has influenced markets and curtailed some of the immediate risks, although peripheral countries continue to struggle.
- The UK's safe haven status and minimal prospect of rate rises are expected to keep gilt yields (and hence PWLB rates) at low rates for the foreseeable future.

2. The Council's Investments

2.1 At 30th November 2012 the council held the following investments:

Investment	Term	Maturity Date	Interest Rate	Amount invested	
				£m	£m
<u>Instant Access Bank Accounts:</u>					
National Westminster	N/A	N/A	1.10%	5.00	5.00
<u>Instant access Money Market Funds:</u>					
Prime Rate	N/A	N/A	0.52%	4.52	
Ignis	N/A	N/A	0.53%	4.87	
Deutsche	N/A	N/A	0.42%	2.00	11.39
<u>Fixed Term Deposits:</u>					
Lloyds	100 days	07/02/13	1.40%	2.00	
Lancashire C C	364 days	06/03/13	0.85%	2.00	
Bank of Scotland	120 days	15/03/13	1.20%	2.00	
Bank of Scotland	120 days	20/03/13	1.20%	1.00	
Bank of Scotland	136 days	22/03/13	1.40%	2.00	
Lloyds	182 days	31/05/13	1.00%	0.50	
Barclays	365 days	01/11/13	1.07%	2.00	
Gateshead Council	549 days	18/11/13	1.10%	2.00	
Barclays	549 days	29/11/13	1.00%	1.00	14.50
<u>Certificate of Deposit:</u>					
Nationwide	32 days	17/12/12	0.40%	1.00	1.00
Total			0.89%		31.89

Shaded lines are term deposits placed between 30/09/12 and 30/11/12 (i.e. since last report)

- 2.2 Since the beginning of the year the council's eligible UK counterparties, together with the maximum maturity periods (as recommended by the council's treasury advisers Arlingclose), have been as follows:

	Date revised					
	1 st Apr	3 rd May	18 th May	1 st Jun	30 th Jul	31 st Oct
Santander UK	35 days	35 days	overnight	overnight	35 days	100 days
Nat West and RBS	100 days	35 days	35 days	overnight	35 days	6 months
Bank of Scotland and Lloyds TSB	100 days	35 days	35 days	overnight	100 days	6 months
Nationwide	100 days	100 days	100 days	100 days	100 days	12 months
Barclays	100 days	100 days	100 days	100 days	100 days	12 months
HSBC and Standard Chartered Bank	6 months	6 months	6 months	6 months	12 months	12 months

- 2.3 Limits were increased from 31st October 2012 due to the creditworthiness of institutions showing signs of stabilisation and, in some cases, considerable improvement.
- 2.4 The rates of interest receivable on the council's investments have continued to fall. For example, interest rates on the following investments have been as follows:

Investment		2 nd Apr	2 nd Jul	28 th Sep	27 th Dec
Prime Rate Money Market Fund (instant access)		0.87%	0.69%	0.61%	0.46%
Ignis Money Market Fund (instant access)		0.82%	0.72%	0.65%	0.50%
Nationwide	E.g. 3 month term deposit	0.98%	0.60%	0.51%	0.44%
Barclays	E.g. 3 month term deposit	0.91%	0.83%	0.53%	0.46%
Lloyds Group	E.g. 3 month term deposit	1.40%	1.40%	1.35%	0.70%

- 2.5 the above indicates that some banks have significantly cut rates in the last few months.
- 2.6 On the recommendation of Arlingclose, the council has opened a custody account so that the council has the option to use a number of alternative approved investment instruments and diversify the investment portfolio. Such instruments include Treasury Bills, Certificates of Deposit and Gilts.
- 2.7 In November the supplier of the custody account announced that they were entering the market for local authority lending. This is of real benefit to the council as the commission charged on borrowing is 0.03% per annum compared to 0.10% traditionally charged by brokers.
- 2.8 Arlingclose has issued the following forecast of the Bank Base Rate (issued 14th December 2012). As previously noted, Arlingclose believe that it could be 2016 before the first increase in the Bank Base Rate.

Bank Rate	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun 15
Upside risk			+0.25	+0.25	+0.25	+0.25	+0.50	+0.50	+0.50	+0.50
Central case	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk		-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25

There is no change in the above forecast from that previously reported.

2.9 The council has earned interest on its investments as follows:

Month	Amount invested		Average rate of interest earned		Amount of interest earned £	Budget £	Short-fall £
	Actual £m	Budget £m	Actual %	Budget %			
Apr-12	22.11	30	1.15	0.90%	20,643	22,500	(1,857)
May-12	31.94	40	1.09	0.90%	29,247	30,000	(753)
Jun-12	32.57	45	1.07	0.90%	28,657	33,750	(5,093)
Jul-12	32.34	50	0.93	0.90%	25,676	37,500	(11,824)
Aug-12	31.33	45	0.98	0.90%	26,190	33,750	(7,560)
Sep-12	28.82	45	1.00	0.90%	23,542	33,750	(10,208)
Oct-12	28.00	45	1.00	0.90%	23,760	33,750	(9,990)
Nov-12	25.61	40	0.98	0.90%	20,505	30,000	(9,495)
Total to 30 November 2012					198,220	255,000	(56,780)
Dec-12	25.00	35		0.90%	18,000	26,250	(8,250)
Jan-13	25.00	35		0.90%	18,000	26,250	(8,250)
Feb-13	21.00	30		0.90%	16,000	22,500	(6,500)
Mar-13	15.00	30		0.90%	13,000	22,500	(9,500)
Projected outturn					263,220	352,500	(89,280)

- 2.10 The interest received in the eight months to 30th November 2012 has fallen short of the amounts budgeted by £56,780. Whilst the average rates achieved each month have been higher than the budgeted rate of 0.90% the average amounts invested have been lower.
- 2.11 The investment budget was set on a consistent basis with the borrowing budget assuming that the council may take out further borrowing totalling £11.5 million at the end of 2011/12 and/or at the beginning of 2012/13. The postponement of this borrowing has caused investment income to fall but the reduction in income is outweighed by savings made on the borrowing side.
- 2.12 In view of falling interest rates, and continuing restrictions on the maximum maturity periods with some banks, actual investment income may fall short of the amount budgeted by around £90,000. This is a further deterioration since the last forecast at the end of September of a £75,000 shortfall.

3. The Council's Borrowing

Short-term borrowing

3.1 During the first eight months of the year the council has taken out short-term loans from other local authorities as follows:

Date Borrowed	Local Authority	£m	Period (days)	Date Repayable	Interest Rate – gross including brokers commission	Interest Payable (including brokers commission)
01/05/12	Worcestershire	3.00	7	08/05/12	0.39%	£224.38
02/05/12	Rhondda	3.97	8	10/05/12	0.39%	£339.35
08/05/12	Worcestershire	3.50	7	15/05/12	0.39%	£261.78
10/05/12	Coventry	3.50	21	31/05/12	0.38%	£765.21
28/05/12	Caerphilly	3.00	10	07/06/12	0.38%	£312.33
24/08/12	Leicester	2.00	83	15/11/12	0.36%	£1,637.27
24/08/12	London Borough of Hammersmith & Fulham	2.00	52	15/10/12	0.37%	£1,054.25
12/09/12	East Renfrewshire	2.00	50	01/11/12	0.37%	£1,013.70
15/10/12	Worcestershire	2.00	50	04/12/12	0.37%	£1,013.70
19/11/12	Leicester City	1.50	28	17/12/12	0.37%	£425.75
20/11/12	West Mercia Police	1.00	56	12/01/13	0.37%	£567.68
26/11/12	Merseyside Transport	2.00	224	08/07/13	0.40%	£4,909.59
30/11/12	South Yorkshire	2.00	255	12/08/13	0.42%	£5,868.49
30/11/12	Merseyside Transport	2.00	283	09/09/13	0.44%	£6,823.02
Total interest and commission payable on loans taken out to 30th November 2012						£25,216.50
Less interest and commission relating to 2013/14						£9,090.41
Total short-term interest for 2012/13 on loans taken out to 30th November 2012						£16,126.09
Shaded lines are those loans repaid as at 30 th November 2012						

3.2 it is good practice to use short term loans to provide additional liquidity at a time when balances were relatively low. More recent borrowing has been to fund capital expenditure.

3.3 It is anticipated that further short-term borrowing will be taken out before the year end. In previous years the council has utilised internal borrowing to finance the capital programme. This was done due to the large cost of carry of investments (the difference between interest paid on PWLB loans and interest earned on investments) and the high credit risk involved.

Long-term borrowing

- 3.4 No long-term loans have been taken out in the year to date.
- 3.5 There are currently good reasons to postpone further borrowing from the Public Works Loan Board (PWLB), including:
- The expectation that PWLB rates will remain low for some months to come;
 - The large differential between PWLB rates and the amount currently earned on the council's investments;
 - The availability of cheap short-term loans from other local authorities; and
 - The flexibility offered by short-term borrowing in terms of repaying loans and reducing investments should financial conditions deteriorate.
- 3.6 The council's borrowing budget was based on taking out new PWLB loans of £11.50 million. However, Arlingclose is forecasting that PWLB rates will remain at relatively low levels for the foreseeable future. Therefore the current strategy is to utilise cheaper short-term loans from other local authorities.
- 3.7 It is anticipated that at the year end the council will have short-term loans outstanding but the difference in the budgeted PWLB interest rate of 4.00% and the interest rates payable on the short-term loans (less than 0.40%) will result in significant budget savings. The current underspend can be estimated as follows:

Summary of Borrowing Budget	Budget	Forecast	Saving
	£m	£m	£m
Minimum Revenue Provision	9.95	9.79	0.16
Interest on existing loans (January 2012 position)	5.76	5.76	-
Provision for borrowing of £5.50m to be taken out before the end of 2011/12 at 4.00%	0.22	-	0.22
Borrowing requirement for 2012/13 of £6m, included at an interest rate of 4.00%	0.24	-	0.24
Interest payable on short-term borrowing in lieu of longer-term loans		0.02	(0.02)
Additional budget towards property disposal costs	0.05	0.05	-
Original budget	16.22	15.62	0.60
Budget adjustment relating to a reduction in capital financing contributions from directorates	(0.15)	-	(0.15)
Forecast budget surplus as at 31 March 2013	16.07	15.62	0.45

4. Summary of Outturn Position

- 4.1 The outturn position will depend upon the timing of any new longer term borrowing. However, assuming that no PWLB borrowing is taken out before the year end and all borrowing is from other local authorities, the current forecast is for an underspend of £360,000. The underspend comprises a borrowing underspend of £450,000, as detailed above, but a shortfall on interest earned of around £90,000.
- 4.2 The council is able to capitalise interest costs relating to interest paid on borrowing used to fund large capital schemes that take substantial periods of time to get to the point at which the assets may be utilised. Such interest, incurred at the construction or installation phase, may be added to the cost of the associated asset. It is difficult to provide an estimate at this stage, however, any interest that the council is able to capitalise will increase the underspend noted above.
- 4.3 The use of short term loans will continue to be a key part of our treasury management and means we are able to deliver savings against this year's revenue budget for funding the capital programme.