

This report ensures the council demonstrates best practice in accordance with CIPFA's recommendations in their 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 first estimate of economic growth for the fourth quarter of 2012 showed the economy contracting by 0.30% over the quarter and by 0% year on year. Although contraction was expected the result was weaker than forecast.
- The Office of Budget Responsibility's forecast for 2013 is for the UK economy to grow by 1.3%.
- The year-on-year Consumer Price Index (CPI) for December 2012 stayed constant at 2.70% for the third month in succession.
- Members of the Monetary Policy Committee voted unanimously to hold the Bank Rate at 0.50% at their meeting in January.
- The US economy managed to steer away from the so called "fiscal cliff" however this issue will resurface in March when a package of spending cuts are due to take effect. However, in the interim the measures taken have been sufficient to see a significant increase in the price of equities and a corresponding fall in the price of gilts (resulting in increased yields and higher PWLB rates).

2. The Council's Investments

2.1 At 31st December 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	0.46%	3.26	
Ignis	N/A	N/A	0.48%	1.05	4.31
<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	
Nationwide	273 days	11/09/13	0.76%	2.00	
Barclays	365 days	01/11/13	1.07%	2.00	
Gateshead Council	549 days	18/11/13	1.10%	2.00	
Barclays	364 days	29/11/13	1.00%	1.00	
Barclays	365 days	05/12/13	1.00%	1.00	17.50
Total			1.00%		26.81

Shaded lines are term deposits placed in December (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 The rates of interest receivable on the council's investments have reduced in the nine months to December 2012. For example, as noted in the previous report, 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%

- 2.4 Current rates at the beginning of February are still at around the levels noted at the end of December.
- 2.5 Arlingclose has issued the following forecast of the Bank Base Rate (issued 18th January 2013). 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.

2.6 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)
Dec-12	31.17	35	0.92	0.90%	24,386	26,250	(1,864)
Total to 31st December 2012					222,606	281,250	(58,644)
Jan-13	25.00	35	0.90	0.90%	18,750	26,250	(7,500)
Feb-13	20.00	30	0.90	0.90%	15,000	22,500	(7,500)
Mar-13	20.00	30	0.90	0.90%	15,000	22,500	(7,500)
Projected outturn					271,356	352,500	(81,144)

2.7 The interest received in the nine months to 31st December 2012 has fallen short of the amounts budgeted by £58,644. Whilst the average rates achieved each month have been higher than the budgeted rate of 0.90%, the average amounts invested have been lower.

2.8 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. Recent short-term borrowing from other local authorities will reduce the gap between projected and actual investment balances but falling council reserves have the opposite effect.

2.9 In view of falling interest rates, and continuing restrictions on the maximum maturity periods with some banks, actual investment income is anticipated to fall short of the amount budgeted by between £70,000 and £90,000.

3. The Council's Borrowing

Short-term borrowing

- 3.1 During the year to date the council has taken out short-term loans from other local authorities. This is good practice as the rates are below levels available from other sources.

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
04/01/13	City & County of Swansea	2.00	97	11/04/13	0.35%	£1,860.27
05/01/13	City & County of Swansea	2.00	92	08/05/13	0.40%	£2,016.43
06/02/13	Kent Police Authority	2.00	119	05/06/13	0.40%	£2,608.22
Total interest and commission payable on loans taken out to 6th February 2013						£25,216.50
Less interest and commission relating to 2013/14						£11,517.81
Total short-term interest for 2012/13 on loans taken out to 6th February 2013						£16,126.09
Shaded lines are those loans both taken out and repaid in 2012/13						

- 3.2 Short-term loans taken out during the year have either been to provide additional liquidity (at times when it was cheaper to use short-term loans to provide liquidity rather than keep instant access to the required investment balances) or, more recently, to fund capital expenditure.

- 3.3 The council can only borrow up to its Capital Financing Requirement and cannot borrow beyond this to finance the revenue budget.
- 3.4 The council's longer term loans from the Public Works Loan Board (PWLB) are all at fixed rates with an average interest rate payable of 4.04%. Short-term loans are currently available at very low rates and remove the cost of carry (the differential between investment and borrowing rates) associated with longer term loans.
- 3.5 At the present time, with the bank base rate anticipated to stay at 0.50% for the next few years, it is intended to use short-term borrowing from other local authorities to fund both this year's capital expenditure and a significant part of the capital expenditure in 2013-14. It can be seen from the above table that the short-term borrowing has been taken out so that £2 million matures each month from April to September inclusive. This is to spread interest rate risk and give the council the opportunity to renew the loans at a time when other local authorities balances should be relatively high resulting in advantageous interest rates. Assuming current rates continue, the council should be able to rollover these loans and borrow for up to one year at a gross interest rate including commission of below 0.60%.

It is stressed that using other local authorities is sound financial management given the very favourable rates available.

Long-term borrowing

- 3.6 No long-term loans have been taken out in the year to date.
- 3.7 As noted previously, there are currently good reasons to postpone further borrowing from the PWLB, including:
- The expectation that PWLB rates will remain relatively low for the foreseeable future;
 - The large differential between PWLB rates and those 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.
- 3.8 As noted in 1.1, longer dated PWLB rates have increased in the last month or so following the United States temporarily avoiding the "fiscal cliff" but given that the "cliff" will resurface in March (when a further \$110 billion of spending cuts are due to take effect), together with the availability of cheap, shorter term borrowing, it is difficult to make a compelling case for replacing one with the other at present.
- 3.9 The costs and benefits of longer term borrowing, relative to shorter term borrowing, will continue to be monitored and discussed with the council's treasury adviser Arlingclose.
- 3.10 It is anticipated that at the year end the council will have £12 million of short-term loans outstanding (as shown in the table above) but the difference in the budgeted PWLB interest rate of 4.00% and the interest rates payable on the short-term loans (less than 0.44% or less) 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 It is anticipated that no PWLB borrowing will be taken out before the year end and all borrowing will consist of short-term loans from other local authorities. The current forecast is for an underspend of £710,000. The underspend comprises:

	£m
Investment income receivable less than budgeted	(0.09)
Interest payable on borrowing less than budgeted	0.45
Capitalisation of interest paid (see below)	0.35
Total underspend	0.71

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. At this stage capitalised interest is estimated to be £350,000, as shown 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.