

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 second estimate of economic growth for the fourth quarter of 2012 confirmed the first estimate with the economy contracting by 0.30% over the quarter. However, upward revisions to growth data in earlier quarters of 2012 lifted year on year growth in GDP from zero to 0.30%.
- The weakness in growth was a major factor in the credit rating agency Moody's downgrading the UK's long term rating from Aaa to Aa1.
- The year-on-year Consumer Price Index (CPI) for January 2013 stayed constant at 2.70% for the fourth month in succession.
- Members of the Monetary Policy Committee voted unanimously to hold the Bank Rate at 0.50% at their meeting in February but were split 6-3 on maintaining the stock of asset purchases at £375 billion. Three members voted to increase the size of the asset purchase programme by £25 billion to £400 billion.
- Political events in Italy cast a shadow over markets as concerns over the Eurozone were raised again.
- The IMF has said that the global economy will slow this year unless the United States averts the spending cuts due to start on 1<sup>st</sup> March.

**2. The Council's Investments**

2.1 At 31<sup>st</sup> January 2013 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	
Santander	N/A	N/A	0.50%	4.49	9.49
<u>Instant access Money Market Funds:</u>					
Prime Rate	N/A	N/A	0.47%	2.48	2.48
<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
<b>Total</b>			<b>0.96%</b>		<b>29.47</b>

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- 2.2 Due to the cessation of council tax receipts, and the need to keep funds liquid in February and March, no new term deposits were placed in January.
- 2.3 The council's current eligible UK counterparties, together with the maximum maturity periods (as recommended by the council's treasury advisers, Arlingclose) are as follows:

	Date counterparty added or maturity limits revised						
	1 <sup>st</sup> Apr	3 <sup>rd</sup> May	18 <sup>th</sup> May	1 <sup>st</sup> Jun	30 <sup>th</sup> Jul	31 <sup>st</sup> Oct	1 <sup>st</sup> Mar
Close Brothers Ltd							100 days
Santander UK	35 days	35 days	overnight	overnight	35 days	100 days	100 days
Nat West and RBS	100 days	35 days	35 days	overnight	35 days	6 mnths	6 mnths
Bank of Scotland and Lloyds TSB	100 days	35 days	35 days	overnight	100 days	6 mnths	6 mnths
Nationwide	100 days	100 days	100 days	100 days	100 days	12 mnths	12 mnths
Barclays	100 days	100 days	100 days	100 days	100 days	12 mnths	12 mnths
HSBC and Standard Chartered Bank	6 mnths	6 mnths	6 mnths	6 mnths	12 mnths	12 mnths	12 mnths

- 2.4 Following a sustained stabilisation in UK credit markets, with effect from 1<sup>st</sup> March Arlingclose have added Close Brothers as a counterparty for short-term, liquid investments. Close Brothers has a long-term credit rating of A and has maintained a relatively stable credit rating throughout the financial crisis. With the UK government keen to reduce the banking sector's reliance on government support Arlingclose are undertaking a detailed analysis of other financial institutions with a standalone strong long term credit rating which does not factor in any government assistance.
- 2.5 The rates of interest receivable on the council's investments have reduced during 2012/13. For example, as noted in the previous report, rates on the following investments have been as follows:

Investment		2 <sup>nd</sup> Apr	2 <sup>nd</sup> Jul	28 <sup>th</sup> Sep	27 <sup>th</sup> 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%

- 2.6 The interest rates on the council's instant access bank accounts have also fallen recently as follows:

Bank	With effect from	Old rate	New rate
Santander	4 <sup>th</sup> December 2012	0.80%	0.50%
Nat West	12 <sup>th</sup> February 2013	1.10%	0.60%
Bank of Scotland	22 <sup>nd</sup> April 2013	0.85%	0.40%

- 2.7 Arlingclose has issued the following forecast of the Bank Base Rate (issued 15<sup>th</sup> February 2013). As previously noted, Arlingclose believe that it could be 2016 before the first increase in the Bank Base Rate.

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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	+0.50	+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

The only slight change from their previous forecast is that there is now no upside risk until March 2014.

2.8 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)
Jan-13	32.04	35	0.92	0.90%	24,831	26,250	(1,419)
<b>Total to 31<sup>st</sup> January 2013</b>					<b>247,437</b>	<b>307,500</b>	<b>(60,063)</b>
Feb-13	28.88	30	0.86	0.90%	19,124	22,500	(3,376)
Mar-13	24.00	30	0.80	0.90%	16,000	22,500	(6,500)
<b>Projected outturn</b>					<b>282,561</b>	<b>352,500</b>	<b>(69,939)</b>

2.9 The interest received in the ten months to 31<sup>st</sup> January 2013 has fallen short of the amounts budgeted by £60,063. Whilst the average rates achieved in this period have been higher than the budgeted rate of 0.90%, the average amounts invested have been lower.

2.10 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.

2.11 In view of falling interest rates, actual investment income is anticipated to fall short of the amount budgeted by around £70,000.

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**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.

<b>Date Borrowed</b>	<b>Local Authority</b>	<b>£m</b>	<b>Period (days)</b>	<b>Date Repayable</b>	<b>Interest Rate – gross including brokers commission</b>	<b>Interest Payable (including brokers commission)</b>
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
<b>Total interest and commission payable on the above loans</b>						<b>£25,216.50</b>
<b>Less interest and commission relating to 2013/14</b>						<b>£11,517.81</b>
<b>Total short-term interest for 2012/13 on loans taken out to date</b>						<b>£16,126.09</b>
Shaded lines are those loans both taken out and repaid in 2012/13						

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- 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 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 existing 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. 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 The costs and benefits of longer term borrowing, relative to shorter term borrowing, continue to be monitored and discussed with the council's treasury adviser Arlingclose. At present their advice is to continue using short-term loans and delay taking out more expensive longer-term finance.
- 3.9 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:

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<b>Summary of Borrowing Budget</b>	<b>Budget</b>	<b>Forecast</b>	<b>Saving</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
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	-
<b>Original budget</b>	<b>16.22</b>	<b>15.62</b>	<b>0.60</b>
<b>Budget adjustment relating to a reduction in capital financing contributions from directorates</b>	<b>(0.15)</b>	<b>-</b>	<b>(0.15)</b>
<b>Capitalised interest</b>		<b>(0.40)</b>	<b>0.40</b>
<b>Forecast budget surplus as at 31 March 2013</b>	<b>16.07</b>	<b>15.22</b>	<b>0.85</b>

**4. Summary of Borrowing 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 £850,000.
- 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. At this stage capitalised interest is estimated to be £400,000, 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.