

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 Office for Budget Responsibility (OBR) has reduced its GDP forecast of growth from 1.2% to 0.6% for 2013 and from 2.0% to 1.8% for 2014.
- The OBR slightly increased its inflation forecast due to higher oil and import prices.
- The year-on-year Consumer Price Index (CPI) for February 2013 increased from 2.7% in previous months to 2.8%.
- The UK outlook for bringing down the structural deficit and stabilising debt levels has deteriorated with the deficit expected to remain around the 2011/12 level of £120 billion for this and the next financial year.
- Members of the Monetary Policy Committee voted unanimously to hold the Bank Rate at 0.50% at their meeting in February but were again split 6-3 on maintaining the stock of asset purchases at £375 billion. As before, three members voted to increase the size of the asset purchase programme by £25 billion to £400 billion.
- The Eurozone recession appears to be deepening. The Italian elections and Cypriot bailout indicate that significant political risks remain to the future economic health of the region.

2. The Council's Investments

2.1 At 28th February 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	0.60%	4.44	
Santander	N/A	N/A	0.50%	4.16	8.60
<u>Fixed Term Deposits:</u>					
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	15.50
Total			0.88%		24.10

2.2 In February and March the direct debit scheme for the Council Tax does not operate. As a result, no new term deposits have been placed since December 2012 so that we maintain adequate cashflow funding.

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						
	1st Apr	3rd May	18th May	1st Jun	30th Jul	31st Oct	1st 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 As noted in the previous report, Arlingclose have added Close Brothers as a counterparty for short-term, liquid investments. At the present time the only investment product offered by Close Brothers is a one month notice account paying 1% but the rate is attractive when viewed against other available rates (with Nationwide, Barclays and HSBC paying less than 1% for a one year term deposit).

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	2nd Apr	2nd Jul	28th Sep	27th 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%

Rates today are at the same levels as at the end of December except that the rate receivable on Ignis Money Market Fund has fallen back to 0.44%.

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

Bank	With effect from	Old rate	New rate
Santander	4 th December 2012	0.80%	0.50%
Nat West	12 th February 2013	1.10%	0.60%
Bank of Scotland	22 nd April 2013	0.85%	0.40%
Royal Bank of Scotland	9 th May 2013	1.10%	0.70%
Barclays	25 th March 2013	0.50%	0.65%

(Since the January report both the Royal Bank of Scotland and Barclays have reduced the rate of interest on their instant access accounts)

2.7 The reduction in the rates of interest offered is a reflection of reduced demand for funds by the banks and building societies, mainly as a result of the government's Funding for Lending Scheme with cheaper funds being available from the Bank of England.

2.8 Arlingclose has issued the following forecast of the Bank Base Rate (issued 21st March 2013). As previously noted, Arlingclose believe that it could be 2016 before the first increase in the Bank Base Rate.

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

There is no change from their February forecast although Arlingclose have noted that the political situation in the Eurozone and US suggest that current risks are on the downside and there is likely to be considerable volatility in gilt yields (and hence PWLB rates).

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)
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)
Feb-13	28.88	30	0.87	0.90	19,265	22,500	(3,235)
Total to 28th February 2013					266,702	330,000	(63,298)
Mar-13	17.00	30	0.91	0.90	13,150	22,500	(9,350)
Projected outturn					279,852	352,500	(72,648)

2.10 The 2012/13 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. Short-term borrowing from other local authorities reduces the gap between projected and actual investment balances but falling council reserves have the opposite effect.

3. The Council's Borrowing

Short-term borrowing

3.1 During the year to date the council has taken out short-term loans at very low levels of interest 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 the above loans						£31,701.42
Less interest and commission relating to 2013/14						£11,649.85
Short-term interest and commission for 2012/13 on loans taken out to date						£20,051.57
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 rather than keep instant access to the required investment balances) or 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 difference 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 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 Because the 2012/13 borrowing budget was set assuming that the council would take out longer term PWLB loans at an interest rate of 4.00%, the use of short-term loans by the council's treasury management team has resulted in significant budget savings that has helped the overall position. 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)
Capitalised interest		(0.40)	0.40
Forecast budget surplus as at 31 March 2013	16.07	15.22	0.85

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 £850k.
- 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 £400k, 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.