

## TRAFFORD BOROUGH COUNCIL

**Report to:** Executive 24 June 2013  
Accounts & Audit Committee 27 June 2013  
Council Meeting 10 July 2013

**Report for:** Decision

**Report of:** The Executive Member for Finance and the Director of Finance

### Treasury Management Annual Performance 2012/13 Report

#### Summary

In accordance with the CIPFA Code of Practice, as adopted by the Council, this report has been prepared to review treasury activities for the past financial year.

During 2012/13 the Council complied with its legislative and regulatory requirements, including compliance with all treasury management prudential indicators.

No new borrowings were undertaken in the year to finance the capital programme and at 31 March 2013 the Council's external debt was £100.5m (£100.7m at 31 March 2012) and investments totalled £52.2m (£76.6m at 31 March 2012).

Investment activity undertaken during 2012/13 resulted in the placement of 302 investments totalling £570m spread over 24 institutions. This compares to the 2011/12 activity when 395 investments were placed totalling £624m in 29 institutions.

During the year and as a result of the above actions, a saving against the treasury management budget of £(0.5m) occurred. This was due to increase in investment interest earned of £(0.2m) and savings in external loan interest payable of £(0.3m).

#### Recommendations

That the Executive and the Accounts & Audit Committee advise the Council;

1. of the Treasury Management activities undertaken in 2012/13,
2. that no prudential limits were breached during 2012/13,
3. that both the CIPFA Code of Practice on Treasury Management and CIPFA Prudential Code for Capital Finance were fully complied with.

Contact person for background papers:  
Graham Perkins – Technical Accountant - Extension: 4017

Background papers: None

Relationship to Policy Framework/Corporate Priorities	Value for Money
Financial	In 2012/13 the Council paid loan interest of £5.3m and received £0.7m from money market investments.
Legal Implications:	No legal implications arising from this report
Equality/Diversity Implications	Not applicable
Sustainability Implications	Not applicable
Staffing/E-Government/Asset Management Implications	Not applicable
Risk Management Implications	The monitoring and control of risk underpins all treasury management activities. The main risks are of adverse or unforeseen fluctuations in interest rates and security of capital sums.
Health & Wellbeing Implications	
Health and Safety Implications	Not applicable

## 1. INTRODUCTION AND BACKGROUND

- 1.1 The Council is required through regulations issued under the Local Government Act 2003, to produce an annual treasury report reviewing treasury management activities and the actual prudential and treasury indicators for 2012/13. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).
- 1.2 In 2012/13, the Accounts & Audit Committee together with the Executive and Full Council received the following reports:
- annual treasury strategy for the year ahead (February 2012)
  - mid-year update report (November 2012)
  - annual report describing the activity undertaken compared to the strategy (June 2013 i.e. this report)
- 1.3 The figures in this report are based on the actual amounts borrowed and invested and as such will differ from those stated in the final accounts which are shown in compliance with International Financial Reporting Standards.
- 1.4 The report comprises of the following sections;
- Economic background & impact on the Strategy(Section 2),
  - Treasury Position (Section 3),
  - Borrowing Position (Section 4),
  - Investment Position (Section 5),
  - Prudential and Performance indicators (Section 6),
  - Conclusions and Recommendations (Section 7),
  - Post 2012/13 events update (Section 8),
  - Appendices.

## 2. ECONOMIC BACKGROUND & IMPACT ON 2012/13 STRATEGY

- 2.1 The challenging economic conditions of the previous years continued throughout 2012/13 and a brief summary of the main events which occurred during the year are highlighted below:

### UK: -

- economic growth (GDP) remained relatively static for the year increasing by 0.5% primarily due to the Olympics & Jubilee celebrations,
- consumer expenditure remained subdued,
- exports remained weak especially to the country's biggest customer - the European Union,
- the Monetary Policy Committee (a) increased quantitative easing by £50bn in July to a total of £375bn, (b) maintained Bank Rate at 0.5% and (c) introduced the Funding for Lending Scheme in July. This resulted in cheap credit being made available to banks causing market investment rates to fall sharply in the second half of the year,
- Consumer Price inflation remained above the 2% Government target, starting the year at 3.0% and finishing at 2.8% in March,
- the coalition Government maintained its tight fiscal policy stance against a background of warnings from the credit rating agencies in the event Moody's and Fitch, downgrading the UK's AAA credit rating to AA1 (23/02/13) and AA+ (19.04.13) respectively.

### EU:-

- the sovereign debt crisis continued to dominate the headlines during the year,
- Greece received a second bailout of €110bn in December, payable in tranches depending on their performance with a further third tranche of €30bn also being agreed,
- a major crisis in Cyprus towards the end of the year resulted in a €10bn loan package being agreed,

- Spanish banks received during the summer, a €100bn package of support

Rest of the World:-

- US – GDP growth was close to 3% with signs of the housing market improving starting to appear. The agreement reached on 1<sup>st</sup> January 2013 to avert some of the “fiscal cliff” reduces the risk of a further recession being encountered.
- China - economic growth slowed due to difficulties being experienced in its exports to the western markets.

2.2 Continued uncertainty in the aftermath of the 2008 financial crisis as highlighted above promoted a cautious approach in our operations. With investments continuing to be dominated by counterparty risk considerations and a reduction in market rates due to the Funding for Lending scheme, cash balances continue to attract relatively low returns compared to borrowing rates.

2.3 The expectation for interest rates within the strategy for 2012/13 anticipated low but rising Bank Rate (starting in quarter 4 of 2014) with similar gradual rises in medium and longer term fixed borrowing rates over 2012/13. This forecast rise has now been pushed back to a start in quarter1 2015 at the earliest.

2.4 The actual movement in interest rates when compared to the expectations in the strategy are shown below and a more detailed analysis detailing how investment rates moved during the course of the year is provided at Appendix A;

	<b>2012/13</b>	<b>1 April 2012</b>	<b>31 March 2013</b>	<b>2012/13</b>
	<b>Forecast Average</b>	<b>Actual</b>	<b>Actual</b>	<b>Actual Average</b>
	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>
UK Bank Rate	0.50	0.50	0.50	0.50
Investment Rates				
3 month	0.70	1.03	0.51	0.69
1 Year	1.60	1.86	0.91	1.33
Loan Rates				
5 Year	2.40	2.10	1.75	1.85
25 Year	4.30	4.39	4.07	4.09

For reference, the 2012/13 budget assumed an average investment rate of 1.00% and that any new borrowing would be undertaken at a maximum rate of 5%.

### 3. TREASURY POSITION

3.1 The Council’s debt and investment position is controlled in order to ensure that security of funds and adequate liquidity for revenue and capital activities maintained at all times. This function is undertaken by the Council’s Treasury Management team. Procedures and controls to achieve these objectives are well established both through Member reporting and officer activity.

3.2 The maturity structure of the debt portfolio was as follows:

	<b>31 March 2013 Actual</b>	<b>31 March 2012 Actual</b>
Under 12 months	£3.1m	£0.3m
12 months and within 24 months	£2.4m	£3.1m
24 months and within 5 years	£8.2m	£7.9m
5 years and within 10 years	£15.5m	£14.3m
10 years and above	£71.3m	£75.1m
Total	£100.5m	£100.7m

3.3 The maturity structure of the investment portfolio was as follows:

	31 March 2013 Actual	31 March 2012 Actual
Instant Access	£19.8m	£27.3m
Under 1 year	£32.4m	£49.3m
Total	£52.2m	£76.6m

3.4 At the beginning and end of 2012/13 the Council's treasury position was as follows:

	31 March 2013 Principal	Total	Interest Rate	31 March 2012 Principal	Total	Interest Rate
<b>DEBT</b>						
<b>Fixed rate:</b>						
-PWLB	£44.5m			£44.7m		
-Market	£25.0m	£69.5m	5.55%	£25.0m	£69.7m	5.56%
<b>Variable rate:</b>						
-PWLB	£0m			£0m		
-Market	£31.0m	£31.0m	4.58%	£31.0m	£31.0m	4.58%
<b>Total debt</b>		<b>£100.5m</b>	<b>5.25%</b>		<b>£100.7m</b>	<b>5.26%</b>
<b>Capital Financing Requirement (to finance past capital expenditure)</b>		<b>£147.6m</b>			<b>£132.3m</b>	
<b>Over/ (under) borrowing</b>		<b>(£47.1m)</b>			<b>(£31.6m)</b>	
<b>INVESTMENTS</b>						
- Fixed rate	£32.4m			£49.3m		
- Variable rate	£19.8m			£27.3m		
<b>Total investments</b>		<b>£52.2m</b>	<b>0.88%</b>		<b>£76.6m</b>	<b>1.12%</b>

#### 4. BORROWING POSITION

- 4.1 As at 31 March 2013 the Council's level of external debt was £100.5m, a profile of which can be found at Appendix B. Of this debt, £1.1m is administered on behalf of Greater Manchester Probation Service which leaves £99.4m in respect of the Council's own long term requirement.
- 4.2 During 2012/13 in response to the continuing interest rate differential between the cost of long term debt (4% to 5.5%) and the return available from short term investments (under 1%) and investment counterparty risk, the Council followed a strategy of borrowing internally (using cash backed reserves). This course of action saved the Council £(0.3)m in debt interest in the year and was undertaken in conjunction with advice obtained from the Council's external advisers Sector
- 4.3 No rescheduling on any of the Council's loans was undertaken in the year as the average differential between PWLB new borrowing rates and premature repayment rates of 1% made rescheduling unviable, due to the high the breakage costs (premium) payable.

## **5. INVESTMENT POSITION**

- 5.1 The Council's investment policy is governed by CLG guidance, which was implemented in the annual investment strategy approved by Council on 22 February 2012. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).
- 5.2 The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.
- 5.3 The Council's main bank account, held with the Co-operative Bank, is non-interest bearing and consequently if no investments were undertaken by the Council's in house treasury management team, the Council would lose a substantial amount of income. During 2012/13 an investment rate of return was 0.88% was achieved through proactive investment management generating £(0.7m) of interest, which was 0.49% or £(0.4m) above the comparable performance indicator of the average 7-day London Interbank BID (LIBID) rate, of 0.39% and £(0.2m) above budget.
- 5.4 For reference the total number of investments undertaken in 2012/13 was 302, totalling £570m and 24 institutions were used.
- 5.5 A breakdown of the Council's temporary investments, as at 31 March 2013 is provided at Appendix C for reference.

## **6. PRUDENTIAL AND PERFORMANCE INDICATORS**

- 6.1 Within the Treasury Management Strategy for 2012/13, approval was given to the treasury management prudential & performance indicators for the period 2012/13 – 2015/16. All indicators and benchmarks set for 2012/13 were complied with and details of these are shown in Appendix D.

## **7. CONCLUSIONS AND RECOMMENDATIONS**

- 7.1 All relevant statutory guidelines, the CIPFA Code of Practice on Treasury Management and CIPFA Prudential Code for Capital Finance were fully complied with during 2012/13, including the prudential indicators.
- 7.2 In response to market conditions no new external borrowing was undertaken generating revenue savings of £(0.3m) and due to higher balances than forecasted along with timing differences from income received ahead of requirement, the return on investments was £(0.2m) higher than originally anticipated.
- 7.3 The Executive and the Accounts & Audit Committee advise the Council;
- of the Treasury Management activities for 2012/13,
  - that no prudential limits were breached during 2012/13.

## **8. POST 2012/13 EVENTS UPDATE**

- 8.1 During April and May 2013, two of the three main credit rating agencies, Fitch and Moody's, both revised down their credit ratings assigned to The Co-operative bank to that of sub investment grade. This downgrade was made in reaction of the bank needing to strengthen its long term funding position in response to enhanced regulatory requirements due to be implemented by the end of 2013.
- 8.2 The credit rating agencies took this action despite the bank having both a strong short and medium term funding profile, significantly above that required by the international regulatory requirements and recently, as highlighted in reports issued by YouGov and uSwitches receiving excellent levels of customer service.

- 8.3 In response to the credit rating agencies actions, The Co-operative bank has recognised these findings and has started to address the situation of strengthening its balance sheet.
- 8.4 For a number of years the Council has used the services of the bank for its day to day banking requirements and has, in accordance with the annual Treasury Management Strategy, together with information obtained from Sector the Council's advisers, placed limited investments with the bank. Whilst the credit ratings of the bank has not previously met the minimum required by the Council, special dispensation was offered to The Co-operative in the Strategy reflecting its status as the Council's banker.
- 8.5 In response to Fitch's downgrade in April, pro-active action was undertaken to (a) place no further investments with the bank, (b) remove the bank from the authorised lending list of institutions with whom investments could be placed, (this is the normal course of action adopted in this scenario) and (c) continue to use the bank for Council's transitional banking requirements (day to day activities).
- 8.6 At the time that this internal decision to remove the bank from its list of authorised investment institutions was made, the Council had £4.5m invested with the bank. Since then £1m was repaid on the due date 24 May 2013 with the balance of £3.5m being set to be repaid on maturity on 12 July 2013.
- 8.7 Whilst the Council will continue to have some exposure to the bank arising from its day to day activities, this is not foreseen to be a problem given the bank's strong short term liquidity position. The service the bank undertakes on behalf of the Council is subject to tender and currently options are being evaluated for when the current contract expires in March 2014.

#### **Other Options**

This report has been produced in order to comply with Financial Regulations and relevant legislation and provides an overview of transactions undertaken during 2012/13.

#### **Consultation**

Not applicable.

#### **Reasons for Recommendation**

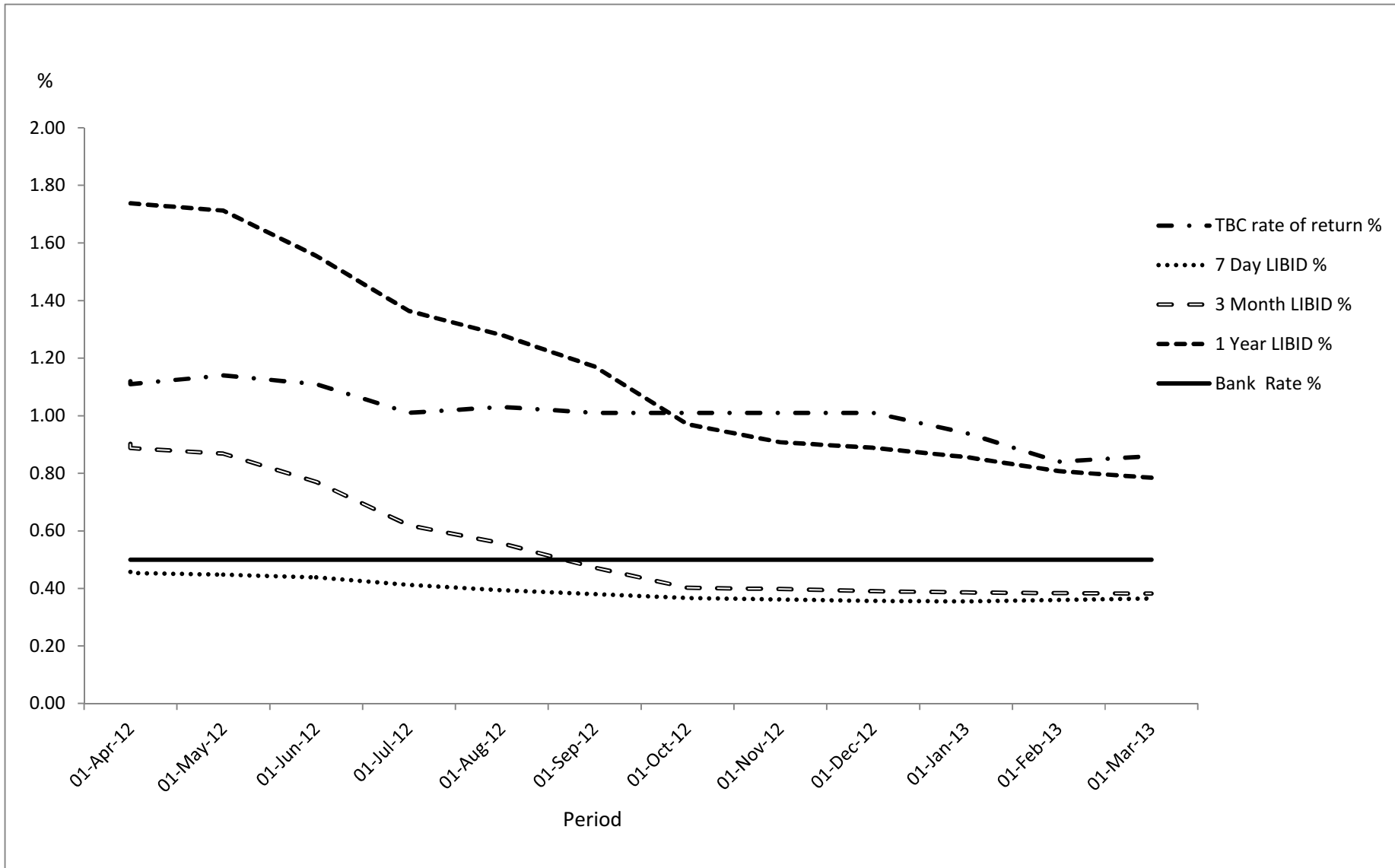
The report meets the requirements of both the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities. The Council is required to comply with both Codes through Regulations issued under the Local Government Act 2003.

**Finance Officer Clearance**      ...ID.....

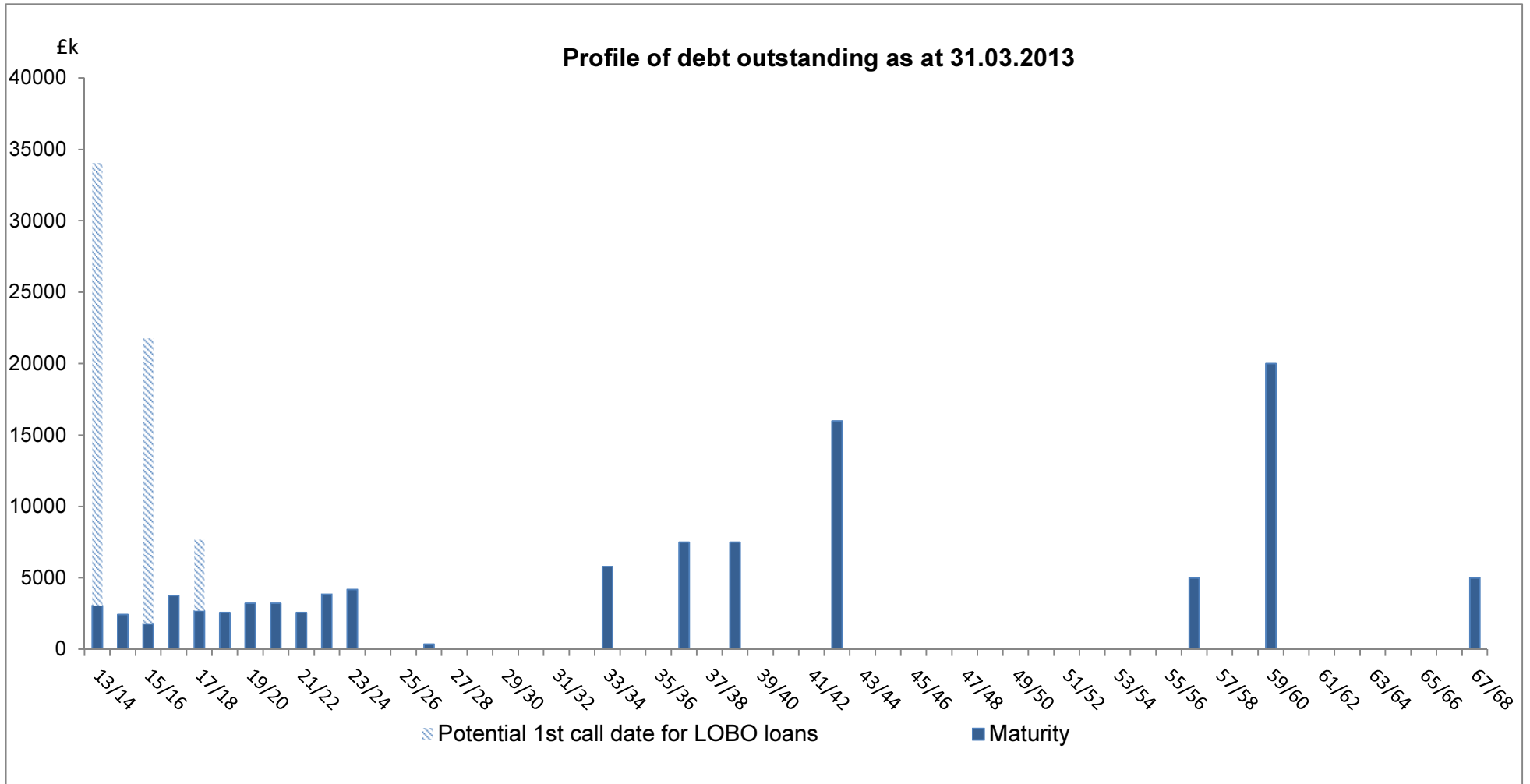
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**Director of Finance Signature Supplied in hard copy.**

### Investment Interest rate movements in 2012-13







## Breakdown of Investments as at 31 March 2013

Counterparty	Amount £	Amount £
<b>UK Institution</b>		
<b>Building Societies</b>		
Nationwide	2,000,000	2,000,000
<b>UK Banks</b>		
Barclays	1,500,000	
HSBC	2,000,000	
Lloyds	16,900,000	
Royal Bank of Scotland	11,500,000	
The Co-operative	1,000,000	32,900,000
<b>Money Market Funds</b>		
Invesco Aim	3,940,189	
Goldman Sachs	420,000	
Ignis	2,000,000	
Legal & General	1,000,000	
Morgan Stanley	2,500,000	
Primerate	2,400,000	12,260,189
<b>Total UK Institutions</b>		<b>47,160,189</b>
<b>Non UK Institutions</b>		
National Bank of Abu Dhabi	5,000,000	5,000,000
<b>Total Non UK Institutions</b>		<b>5,000,000</b>
<b>Grand Total</b>		<b>52,160,189</b>

## Appendix D

### Prudential Indicators for 2012/13

Figures are for the financial year	2012/13 Indicator (max)	2012/13 Actual (max)
<p style="text-align: center;"><b>Authorised Borrowing Limit</b></p> <p>(This is the maximum level of external debt &amp; other long term liabilities (PFI &amp; leases) that the Council requires – this is a statutory limit under Section 3(1) of the Local Government Act 2003.</p>	£156m	£107m
<p style="text-align: center;"><b>Operational Boundary</b></p> <p>(This is calculated on a similar basis as the authorised limit &amp; represents the expected level of external debt &amp; other long term liabilities (PFI &amp; leases) may reach during the year, it is not a limit.</p>	£136m	£107m
<p style="text-align: center;"><b>Upper limits on fixed interest rates</b></p> <p>(Maximum limit of fixed interest rate exposure - debt interest less investment interest)</p>	£4.0m	£3.6m
<p style="text-align: center;"><b>Upper limits on variable interest rates</b></p> <p>(Maximum limit of variable interest rate exposure – debt interest less investment interest)</p>	£1.9m	£1.4m
<p style="text-align: center;"><b>Maturity structure of fixed rate borrowing</b></p> <p>(These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing – these are required for upper, as shown and lower limits which were set at 0%).</p>		
Under 1 year (this includes the next call date for Market loans)	50%	33.9%
1 year to 2 years	50%	22.3%
2 years to 5 years	50%	13.1%
5 years to 10 years	75%	15.4%
10 years to 20 years	75%	4.5%
20 years to 30 years	75%	5.8%
30 years to 40 years	75%	0.0%
40 years and above	75%	5.0%
<p style="text-align: center;"><b>Maximum principal funds invested exceeding 364 days (excluding Manchester International Airport shares)</b></p> <p>(These limits are set to reduce the need for early sale of an investment)</p>	£50.m	£0m

### Performance Indicators for 2012/13

Indicator	Target	Actual
<b>Security</b> – potential default rate of the Council's investment portfolio based on current default rates provided from the 3 main credit rating agencies – its inclusion is recommended by CIPFA.	Max 0.08%	Max 0.02%
<b>Liquidity</b> – investments available within 1 week notice	£20m min.	Achieved
<b>Liquidity</b> – Weighted Average Life of investments	6 months max.	3 months
<b>Yield</b> – Investment interest return to exceed 7 day London Interbank BID rate	0.39%	0.88%
<b>Origin of investments placed</b> - maximum of the Council's investments to be directly placed with non-UK counterparties.	UK institutions 100%	Max 79%
	Non UK institutions 40%	Max 21%