TREASURY MANAGEMENT UPDATE QUARTER 1 (APRIL-JUNE) 2012-13

Purpose:

The Chartered Institute of Public Finance and Accountancy (CIPFA) issued the revised Code of Practice for Treasury Management in November 2009; it recommends that members should be updated on treasury management activities at least twice a year, but preferably quarterly. This report therefore ensures this council is implementing best practice in accordance with the Code.

Economic climate:

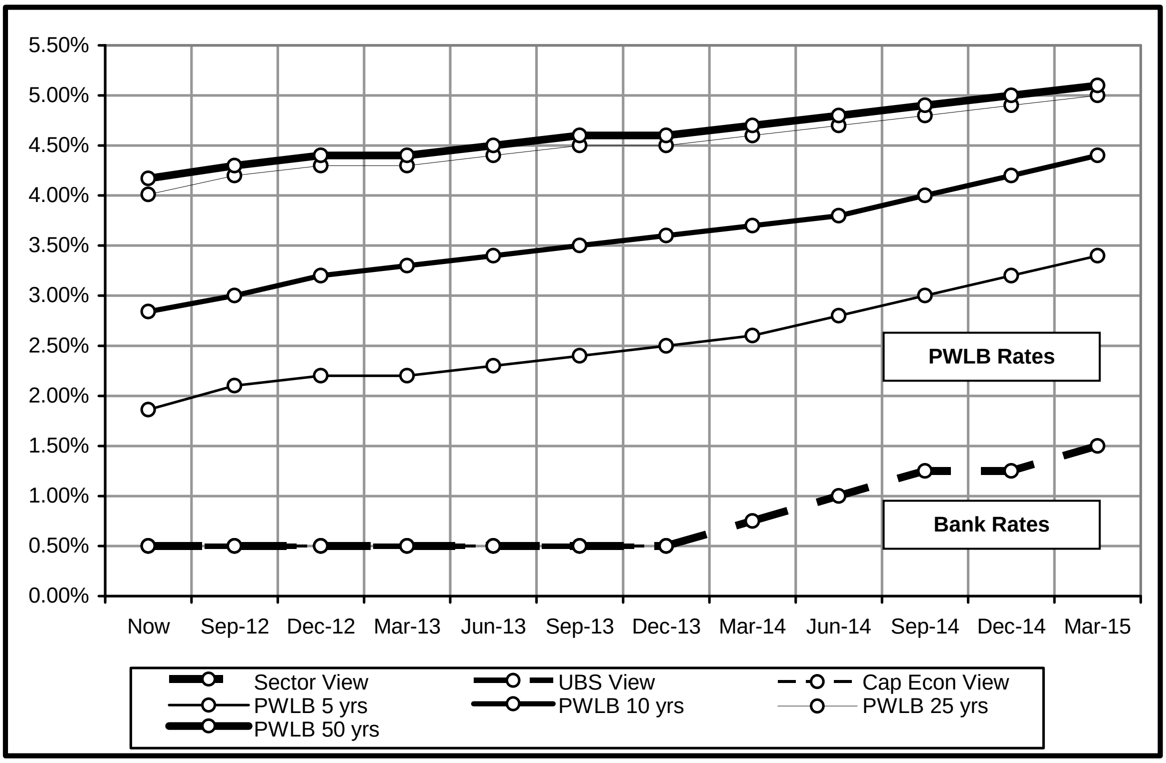
In summary, the second quarter of 2012 (calendar year) saw:

- The economic outlook has generally weakened;
- High street demand was volatile as a result of temporary distortions;
- Employment rose and unemployment fell, but earnings growth remained weak;
- Inflation continued to fall;
- The Bank and the HM Treasury announced measures to help the UK banking sector;
- The MPC indicated another tranche of quantitative easing (QE);
- Gilt yields fell on the back of deteriorating economic data and safe-haven flows from the euro-zone;
- Sentiment towards the Eurozone alternately rose on the announcement of measures to address the crisis, but then fell back as measures disappointed.

Interest rate forecast:

The forecast for interest rates over the next three years (where available) is set out below. The bank rate views of treasury advisors Sector is shown against those of economic analysts Capital Economics and UBS:

	Now	Sept 2012	Dec 2012	Mar 2013	Jun 2013	Sept 2013	Dec 2013	Mar 2014	Jun 2014	Sept 2014	Dec 2014	Mar 2015
Central Bank Rates												
Sector View	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.25%	1.50%
UBS View	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	-	-	-	-	-
Cap Econ View	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	-	-	-	-	-
Public Works Loan Board Rates												
5 yrs	1.86%	2.10%	2.20%	2.20%	2.30%	2.40%	2.50%	2.60%	2.80%	3.00%	3.20%	3.40%
10 yrs	2.84%	3.00%	3.20%	3.30%	3.40%	3.50%	3.60%	3.70%	3.80%	4.00%	4.20%	4.40%
25 yrs	4.01%	4.20%	4.30%	4.30%	4.40%	4.50%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%
50 yrs	4.17%	4.30%	4.40%	4.40%	4.50%	4.60%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%



With growth predictions for the UK continuing to be reduced on an almost monthly basis by both the Office for Budget Responsibility and economic commentators generally, and financial markets unconvinced that Euro-one sovereign debt crisis in the medium-term, we are likely to continue to experience high levels of volatility.

Officer's views are that Bank Rate will continue to be held at record low levels throughout 2013 and the eventual rate rises will subsequently be delayed and potentially at a slower rate than currently forecast. As a result, budget assumptions will include a sensitivity analysis of the impact that a delayed economic recovery would have on the Council.

Annual Investment Strategy

The Treasury Management Strategy Statement (TMSS) for 2012/13, which includes the Annual Investment Strategy, was approved by the Council on 21st February 2012. It sets out the Council's investment priorities as being:

1. **S**ecurity of Capital;
2. **L**iquidity; and
3. **Y**ield

The Council will also aim to achieve the optimum return (yield) on investments commensurate with proper levels of security and liquidity.

In the current economic climate it is considered appropriate to keep the majority of investments short term to cover short term cash flow needs but also to seek out value available in significantly higher rates in periods up to 12 months with highly credit rated financial institutions.

Investment rates available in the market continue to be low. Investment balances at the 31st March 2012 were £101.607m. Due to the front-loaded nature of various government funding streams the average level of funds available for investment purposes during the quarter was £135.9m.

Balances are forecast to fall to circa £85.0m by 31st March 2013 as internal resources are applied to fund capital expenditure demands in lieu of further borrowing, effectively reducing the cost of carrying debt at higher cost than income generated through investment of balances.

Benchmark	**Benchmark Return**	**Council Performance**
3 month	0.87%	1.46%

As illustrated, the authority outperformed the benchmark by 59 basis points. The Council's budgeted investment return for 2012/13 is £0.571m, and performance for the year to date is above target. Latest projections for the financial year are reported through the Budget Monitoring process.

New Borrowing

No new borrowing was undertaken during the quarter.

The Governments Housing Subsidy scheme came to an end on 31st March 2012. In order to exit the scheme and retain future HRA income surplus balances, the Council paid over to CLG the sum of £170.6m financed by new loans from the PWLB taken at the tail end of Q4 2011.

Debt Restructuring

Debt rescheduling opportunities have been limited due to the current economic climate and consequent structure of interest rates following increases in PWLB new borrowing rates in October 2010. Officers continue to monitor the position regularly.

No debt rescheduling was undertaken during the quarter.

Compliance with Treasury and Prudential Limits

It is a statutory duty for the Council to determine and keep under review the affordable borrowing limits. The Council's approved Treasury and Prudential Indicators (affordability limits) were approved alongside the TMSS on 22nd February 2012.

During the financial year to date the Council has operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Management Strategy Statement.

On one occasion the maximum exposure limit the Council internally applies to separate counterparties was exceeded (by 0.07%). This occurred when interest earned on a deposit account balance was compounded along with accumulated principal. The counterparty in question is a part-nationalised highly rated (F1) UK institution, and so the additional risk posed to the authority was minimal. The amount on deposit has since been reduced in line with limits, and measures to strengthen procedures have been implemented.

The Prudential and Treasury Indicators are as follows:

Prudential Indicator	**2012/13 Indicator**	**Quarter 1 – Actual**
Authorised limit for external debt	----- £597.000m	-----
Operational boundary for external debt	----- £577.000m	-----
Gross borrowing	£453.564m	£453.564m
Investments	£95.000m	£138.307m
Net borrowing	£358.564m	£315.257m
Capital Financing Requirement (CFR)	£563.102m	£554.867m
Ratio of financing costs to net revenue streams: GF	12.22%	10.66%
HRA	44.83%	35.22%
Incremental impact of capital investment decisions:-		
a) Increase in council tax (band D) per annum.	£26.10p	£26.10p
b) Increase in average housing rent per week	£0.08p	£0.08p
Limit of fixed interest rates based on net debt (average)	£567.000m	£363.264
Limit of variable interest rates based on net debt (average)	£30.000m	-£48.007
Principal sums invested > 364 days	£30.000m	£5.000m
Maturity structure of borrowing limits:-		
Under 12 months	Max. 15% Min. 0%	3.97%
12 months to 2 years	Max. 15% Min. 0%	3.31%
2 years to 5 years	Max. 50% Min. 0%	9.07%
5 years to 10 years	Max. 50% Min. 0%	4.61%
10 years and above	Max. 100% Min. 50%	79.04%