

<b>Subject:</b>	<b>Treasury Management Policy Statement (incorporating the Annual Investment Strategy) 2010/11 - End of year review</b>		
<b>Date of Meeting:</b>	<b>14 July 2011</b>		
<b>Report of:</b>	<b>Director of Finance</b>		
<b>Lead Member:</b>	<b>Cabinet Member for Finance &amp; Central Services</b>		
<b>Contact Officer:</b>	<b>Name: Peter Sargent</b>	<b>Tel: 29-1241</b>	
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<b>Key Decision:</b>	<b>No</b>		
<b>Wards Affected:</b>	<b>All</b>		

**FOR GENERAL RELEASE****1. SUMMARY AND POLICY CONTEXT:**

- 1.1 The Treasury Management Policy Statement (TMPS) and the Treasury Management Practices (including the schedules) for the year 2010/11 were approved by Cabinet on 11 March 2010. The TMPS sets out the key role for treasury management, whilst the practices and schedules set out the annual targets for treasury management and the methods by which these targets shall be met.
- 1.2 The TMPS includes an annual investment strategy, which sets out the key investment parameters for council cash funds. Full Council approved the investment strategy on 18 March 2010.
- 1.3 The purpose of this report is to advise of the action taken during the second half of the financial year 2010/2011 on the TMPS, including the investment strategy (the action for the first half year was reported to Cabinet on 11 November 2010).

**2. RECOMMENDATIONS:**

- 2.1 That Cabinet endorses the action taken during the second half year to meet the treasury management policy statement and practices (including the annual investment strategy).
- 2.2 That Cabinet notes the maximum indicator for risk agreed at 0.05% has not been exceeded.
- 2.3 That Cabinet notes the authorised limit and operational boundary set by the Council have not been exceeded.

### 3. RELEVANT BACKGROUND INFORMATION/CHRONOLOGY OF KEY EVENTS:

#### Overview of markets

- 3.1 An overview of the market is set out in Appendix 1 to this report. The headline news during the half-year has seen the Bank of England leave the official Bank Rate and quantitative easing programme unchanged, inflation (as measured by the consumer prices index) remaining above the target range and financial difficulties within the Euro area a cause for concern.

#### Treasury Management Strategy

- 3.2 A summary of the action taken in the period October 2010 to March 2011 is provided in Appendix 2 to this report. The main points are:
- two flexible loans totalling £20m agreed in early 2010 became “live” with the cash being received in February 2011
  - a long-term loan valued at £15m was repaid on 1<sup>st</sup> March 2011
  - the level of investments made by the in-house treasury team totalled £32.6m as at 31<sup>st</sup> March 2011, a decrease of £6.9m during the half-year
  - the return on investments has exceeded the benchmark rate for both in-house investments and those undertaken by the cash manager
  - the two borrowing limits approved by the Council – the authorised limit and operational boundary – have not been exceeded.
- 3.3 The council continues to promote its’ ethical investment statement with institutions within which it deposits money. Investment counterparties are advised of the following statement each and every time a deposit is placed with them:

*“Brighton & Hove City Council, in making investments through its treasury management function, fully supports the ethos of socially responsible investments. We will actively seek to communicate this support to those institutions we invest in as well as those we are considering investing in by:*

- *encouraging those institutions to adopt and publicise policies on socially responsible investments;*
- *requesting those institutions to apply council deposits in a socially responsible manner.”*

- 3.4 With effect from April 2010 the council was commissioned by South Downs National Park Authority to provide a range of financial services, including treasury management. In terms of treasury management the Director of Finance advises on the management of risk, has developed an investment strategy and undertakes day-to-day as well as strategic treasury decisions.

#### Budget v Outturn 2010/11

- 3.5 The following table summarises the performance on investments compared with the budgeted position and benchmark.

	In-house investments		Cash manager investments (net of fees)	
	Aver bal	Aver rate	Aver bal	Aver rate
Budget 2010/11	£17.7m	1.28%	£24.0m	1.38%
Actual	£47.2m	0.66%	£24.2m	1.05%
Benchmark rate (i.e. average market rate)	-	0.43%	-	0.43%

- 3.6 There was a marginal overspend on the financing costs budget of circa £26k in 2010/11. The following table (before adjusting for principal repayments and interest on PFI projects) summarises the areas of variance.

Budget 2010/11		£10.510m
Treasury management activity		
○ Reduction in the cost of borrowing	-£0.059m	
○ Higher investment income	-£0.043m	-£0.102m
Other changes not directed related to treasury management activity (e.g. reduction in interest payable on interest reserves & provisions)		+£0.128m
Actual 2010/11		£10.536m

### Summary of treasury activity October 2010 to March 2011

- 3.7 The table below summarises the treasury activity in the half-year to March 2011 with the corresponding period in the previous two years.

	Oct 08 to Mar 09	Oct 09 to Mar 10	Oct 10 to Mar 11
Long-term borrowing raised	£3.0m	£15.0m	£20.0m
Long-term borrowing repaid	(£47.0m)	-	(£15.0m)
Short-term borrowing raised	£21.4m	£138.0m	-
Short-term borrowing repaid	(£21.4m)	(£119.4m)	-
Investments made	£318.9m	£230.0m	£340.4m
Investments maturing	(£408.6m)	(£228.0m)	(£347.3m)

- 3.8 The following table summarises how the day-to-day cash flows in the second half-year have been funded compared to the same period in the previous two years.

	Oct 08 to Mar 09	Oct 09 to Mar 10	Oct 10 to Mar 11
Cash flow shortage	(£46.0m)	(£31.6m)	(£11.9m)
Increase / (decrease) in long-term borrowing	(£44.0m)	£15.0m	£5.0m
Increase / (decrease) in short-term borrowing	-	£18.6m	-
Decrease / (increase) in investments	£89.7m	(£2.0m)	£6.9m
Decrease / (increase) in bank balance	£0.3m	-	-

## Interest rate risk

- 3.9 Cabinet has previously been advised the policy of repaying debt (to reduce investment risk) left the council exposed to the risk of long-term interest rates rising. To protect against this risk three loans were entered into whereby the terms were agreed in advance of cash being received.
- 3.10 Following the Chancellor's announcement on the Spending Review in October 2010 HM Treasury instructed the Public Works Loan Board (PWLB) to increase the average interest rate on all loans raised from 21<sup>st</sup> October. The impact on PWLB rates was an immediate increase across all periods, for example

Period (maturity loans)	20 <sup>th</sup> Oct 2010	21 <sup>st</sup> Oct 2010	Increase
10 years	3.22%	4.08%	+0.86%
20 years	4.08%	4.93%	+0.85%
50 years	4.26%	5.09%	+0.83%

Source: PWLB

- 3.11 The decision to borrow in advance has partially mitigated the increase in cost of borrowing PWLB funds.
- 3.12 During the half-year two of these loans totalling £20m were received. The average cost of these loans is 4.21% and the average period to maturity is 49 years. Details of the loans are set out in Appendix 2.

## Security of investments

- 3.13 A summary of investments made by the in-house treasury team and outstanding as at 31 March 2011 is tabled below. The table shows that investments continue to be held in high quality, short-term instruments.

AA institutions	£6.2m	19%
A institutions	£9.9m	30%
AAA rated money market funds	£16.5m	51%
	£32.6m	100%
Period – less than one month	£24.0m	74%
Period – over one month and less than three months	£6.2m	19%
Period – over three months and less than six months	£2.4m	7%
	£32.6m	100%

## Risk

- 3.14 As part of the investment strategy for 2010/11 the Council agreed a maximum risk indicator of 0.05%. The indicator is a simple target that measures the risk within the investment portfolio based on counterparty risk and length of investment. The indicator is consistent with the investment parameters set out in the investment strategy.

- 3.15 The following table summarises the indicator at the mid-point of each month in the half-year period and confirms investments have been made in high quality counterparties

	Mid month					
	Oct 10	Nov 10	Dec 10	Jan 11	Feb 11	Mar 11
Maximum risk indicator	0.050%	0.050%	0.050%	0.050%	0.050%	0.050%
Risk indicator	0.004%	0.003%	0.005%	0.004%	0.003%	0.002%

#### 4. CONSULTATION

- 4.1 The council's external treasury advisor has contributed to this report.

#### 5. FINANCIAL & OTHER IMPLICATIONS

##### Financial Implications:

- 5.1 The financial implications arising from the action taken under the TMPS are included in Financing Costs. Details of the 2010/11 outturn for financing costs are included under Section 3.6 above.
- 5.2 Cabinet agreed at its meeting in November 2008 to earmark an underspend on Financing Costs to offset the lower investment returns projected over a three year period. As part of the 2011/12 General Fund Budget the reserve was reviewed and, based on projections that indicated the reserve is not expected to be required beyond 2012/13, the sum of £118k was released back to General Reserves. At 31 March 2011 the reserve stood at £1.077million. This reserve will be kept under review and any changes reported back to Cabinet.

*Finance Officer consulted: Peter Sargent Date: 24/06/11*

##### Legal Implications:

- 5.3 The TMPS and action under it must be in accordance with Part I of the Local Government Act 2003 and regulations issued thereunder. Relevant guidance also needs to be taken into account.
- 5.4 This report is for information purposes only and as such it is not considered that anyone's rights under the Human Rights Act will be adversely affected by it.

*Lawyer consulted: Abraham Ghebre-Ghiorgis Date: 24/06/11*

##### Equalities Implications:

- 5.5 No equalities impact assessment is required for this report.

##### Sustainability Implications:

- 5.6 None arising from this report.

Crime & Disorder Implications:

- 5.7 None arising from this report.

Risk and Opportunity Management Implications:

- 5.8 Action taken in the six months to March 2011 is consistent with the risks identified within the TMPS and associated schedules.
- 5.9 In February 2011 the council's Head of Internal Audit & Business Risk undertook an audit of the treasury management function. The audit concluded that "substantial assurance" is provided on the effectiveness of the control framework operating and mitigation of risks for treasury management meaning that effective controls are in place to manage the key risks to the system/service.

Corporate / Citywide Implications:

- 5.10 None arising from this report.

**6. EVALUATION OF ANY ALTERNATIVE OPTION(S):**

- 6.1 This report sets out action taken in the six months to March 2011. No alternative options are therefore considered necessary.

**7. REASONS FOR REPORT RECOMMENDATIONS**

- 7.1 Treasury management is governed by a code that is recognised as 'best and proper practice' under the Local Government Act 2003. The Code requires a minimum of two reports per year, one of which is a report looking back at the closing year. This report fulfils this requirement.

## **SUPPORTING DOCUMENTATION**

### **Appendices:**

1. Appendix 1 – Economic background
2. Appendix 2 – A summary of the action taken in the period October 2010 to March 2011
3. Appendix 3 – Performance and balances
4. Appendix 4 – Prudential indicators 2010/11 Actual

### **Documents In Members' Rooms**

None

### **Background Documents**

1. Part I of the Local Government Act 2003 and associated regulations
2. "The Treasury Management Policy Statement and associated schedules 2010/11" approved by Cabinet on 11 March 2010
3. The "Annual Investment Strategy 2010/11" approved by full Council on 18 March 2010
4. Papers held within Strategic Finance, Finance & Resources
5. "The Prudential Code for Capital Finance in Local Authorities" published by CIPFA 2003 and revised in 2009

