

RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL

MUNICIPAL YEAR 2013-2014

**COMMITTEE:
CORPORATE SERVICES SCRUTINY
COMMITTEE**

AGENDA ITEM NO. 5
TREASURY MANAGEMENT 2012/13 REVIEW

8th October 2013

REPORT OF :

**THE GROUP DIRECTOR, CORPORATE SERVICES
Steve Merritt (01443) 424088**

1.0 PURPOSE OF REPORT

1.1 This report provides Members with the opportunity to scrutinise the Annual Treasury Management Review presented to Council on 24th July 2013 (Appendix 1).

2.0 RECOMMENDATIONS

It is recommended that Members:

2.1 Note the content of this report.

2.2 Scrutinise and comment on the information provided.

2.3 Consider whether they wish to receive further detail on any matters contained in the report.

3.0 ANNUAL TREASURY MANAGEMENT REVIEW (Appendix 1)

3.1 This report details the activities undertaken by the Treasury Management function during 2012/13.

3.2 I would like to highlight key points as follows:

- The Council has complied with all relevant Codes of Practice, regulations and guidance (para 3.3).
- Net Capital Charges for the year were within budget (para 7.3).
- Compliance has been achieved in terms of all Prudential and Treasury indicators (para 8.1).
- The Council continues to adopt a low risk strategy in terms of investing and borrowing (para 9.2).

- The Council continues to receive dividends in respect of the investment in Heritable Bank that defaulted during October 2008 (paras 10.3 – 10.4).

4.0 CONCLUSION

- 4.1 This report, together with Appendix 1 provides Members with the opportunity to scrutinise the 2012/13 activities of Treasury Management.

RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL

MUNICIPAL YEAR 2013-2014

COUNCIL

24th July 2013

REPORT OF :

THE GROUP DIRECTOR, CORPORATE SERVICES
Steve Merritt (01443) 424088

	AGENDA ITEM NO.7
2012/13 ANNUAL TREASURY MANAGEMENT REVIEW	

1.0 PURPOSE OF REPORT

1.1 This report constitutes the statutory requirement to provide Members with information on :-

- the Council's Treasury Management activity during 2012/13; and
- the actual Prudential and Treasury Indicators for 2012/13.

2.0 RECOMMENDATIONS

2.1 It is recommended that Members note the content of this report.

3.0 INTRODUCTION

3.1 Treasury Management is defined as:

"The management of a local authority's cash flows, its borrowings and its investments, the management of the associated risks, and the pursuit of the optimum performance or return consistent with those risks".

3.2 This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (revised 2009 and 2011) and the CIPFA Prudential Code for Capital Finance in Local Authorities (revised 2009 and 2011). The Council is required to comply with both Codes through Regulations issued under the Local Government Act 2003.

3.3 The primary requirements of the Codes are as follows:

- Creation and maintenance of a Treasury Management Policy;

- Creation and maintenance of Treasury Management Practices, which set out the manner in which the Council will seek to achieve stated policies and objectives;
- Approval by Council (by 31st March) of a Treasury Strategy Report (including Prudential and Treasury Indicators and an Investment Strategy) for the year ahead, an Annual Review Report of the previous year and a Mid Year Review; and
- Effective scrutiny of the Treasury Management function.

Rhondda Cynon Taf C.B.C. complies with these requirements and supplements this by including detail of our treasury activities and prudential indicators in the quarterly Council performance reports to Members.

3.4 During 2012/13, the Corporate Services Scrutiny Committee has continued to scrutinise the Treasury Management function via quarterly performance reports and reviews of the strategy and mid year position. To assist Members in discharging this duty, a training session was delivered by Sector, the Council's current Treasury Management advisors during October 2012.

3.5 This annual report will cover the following areas of treasury activity during 2012/13 :

- Treasury Management advisors;
- Economic background;
- Borrowing strategy;
- Borrowing activity and results;
- The estimated and actual treasury position and prudential indicators;
- Investment strategy;
- Investment activity and results.

3.6 It should be noted that the accounting practice to be followed by the Council requires financial instruments in the accounts (debt, investments, etc) to be measured in a method compliant with International Financial Reporting Standards. The figures in this report are based on the principal amounts borrowed and invested and so may differ from those in the Council's Statement of Accounts.

4.0 TREASURY MANAGEMENT ADVISORS

4.1 The Council appointed Butlers (a division of ICAP) as its Treasury Management Advisors during March 2009. During October 2010, the Council received notification from Butlers that it had entered into an agreement with Sector Treasury Services Ltd (a subsidiary of Capita) to transfer its business to Sector. As most staff transferred to Sector, the Council continues to have the same individual as a primary contact.

- 4.2 To date, the service provided has continued to be good and in line with the contract provisions the option has been taken to extend the contract for a further two years until 31st March 2014.
- 4.3 The Council will continue to monitor advisors performance. If any adverse performance or contractual issues arise, Members will be informed accordingly.
- 4.4 The Council recognises that responsibility for Treasury Management decisions remains with the Council.

5.0 ECONOMIC BACKGROUND

5.1 General Economic Background

- 5.1.1 The original expectation for 2012/13 was that the Bank Rate would not rise in 2012/13 or 2013/14 and for it to start rising gently from the end of 2014. This has now been pushed back to quarter one 2015 at the earliest. The Bank Rate remained at 0.5% throughout the year.
- 5.1.2 Economic growth (GDP) in the UK was virtually flat during 2012/13 due to the UK austerity programme, subdued consumer expenditure and weak growth in our biggest export market – the EU. This weak growth resulted in the Monetary Policy Committee (MPC) increasing quantitative easing by £50bn in July to a total of £375bn.
- 5.1.3 Gilt yields remained low for much of the year and this has the impact of reducing PwLB borrowing rates for public bodies. The gilt yields fall as markets sought “safe havens” in government bonds and also due to the impact of increased quantitative easing.
- 5.1.4 Investment rates fell sharply during the second half of the year as the Funding for Lending scheme was introduced. This made cheap credit available for banks for them to lend on.
- 5.1.5 The credit rating agency, Moody’s downgraded the UK’s credit rating from AAA to Aa1 during February. Other agencies attributed a “negative watch” to the government and subsequently Fitch downgraded the UK from AAA to AA+ during April 2013. This was as a result of concerns over the expectations of growth in the economy and a reflection of the challenges faced by the government in its debt reduction programme. Despite the downgrades, both Moody’s and Fitch deemed the outlook as “stable”.
- 5.1.6 The Council continued to maintain a low risk strategy throughout the year to ensure exposure to capital loss was minimised.

5.2 Short term investment rates

5.2.1 The Council's investment income is subject to changes in short term interest rates. The level of the Bank Rate is one of the main determinants of the rate of interest the Council receives on its short term investments. The Bank of England continued to maintain the Bank Rate at 0.5% throughout the year.

5.3 Longer Term interest Rates

5.3.1 The majority of the Council's borrowing is from the PWLB (Public Works Loans Board). Long-term borrowing rates are influenced by gilt yields which are driven by inflation and demand/supply considerations.

5.3.2 Members will recall that local authorities were presented with an unexpected change of policy by the PWLB in October 2010. This resulted in an increase of new borrowing rates of approximately 0.9% without an associated increase in early redemption rates. This makes borrowing more expensive and early repayment less attractive.

5.3.3 During August 2012, HM Treasury introduced "the certainty rate", whereby local authorities are able to access borrowing at 0.2% cheaper than published PWLB rates. In order to access the discounted rate, authorities were required to provide WG (and onward, the Debt Management Office) with an indication of their potential borrowing requirements for the next 3 years.

5.3.4 PWLB rates during 2012/13 were as follows (these are the "certainty rates"):

	5 years	10 years	25 years	50 years
Average	1.76%	2.79%	4.01%	4.17%
Highest	2.15%	3.28%	4.39%	4.43%
Lowest	1.48%	2.46%	3.76%	3.91%

6.0 BORROWING STRATEGY

6.1 The borrowing strategy for 2012/13 approved by Council in March 2012 stated that the borrowing requirement to fund the 2012/13 Capital Programme was £20m. In line with the capital programme, the borrowing requirement increased to £21m during the year. It was also reported that the cheapest borrowing will be "internal borrowing" by running down cash balances and foregoing interest earned at historically low rates. This also minimises counterparty risk (risk that an investment may become irrecoverable).

6.2 The strategy also reported that the Section 151 Officer, under delegated powers, will take the most appropriate form of borrowing

depending upon the prevailing interest rates at the time, taking into account advice provided by our advisors.

- 6.3 It was also reported that the Council may reschedule debt where there is an opportunity to generate savings. However, as stated in paragraph 5.3.2 above, changes in PWLB rates calculations has reduced the attractiveness of early repayments associated with rescheduling.

7.0 BORROWING ACTIVITY AND RESULTS

- 7.1 A summary of the Council's borrowing activity (excludes PFI and Finance Leases) can be seen in the table below:

£'M	Fixed Rate Debt	Market Debt	Variable Debt	Total
Opening Bal 1st April 2012	118.119	87.500	0.782	206.401
Repayments	(8.145)	0	(0.129)	(8.274)
New borrowing for 2012/13	0	0	0.151	0.151
Closing Bal 31st March 2013	109.974	87.500	0.804	198.278

- 7.2 In accordance with our low risk strategy as detailed in section 6 above, to minimise investment exposure and counterparty risk on cash balances held, no long term borrowing was undertaken during 2012/13.
- 7.3 During the year there was a net saving on the Council's Net Capital Charge Budget (£23.6m) of £0.096m. This has been achieved as a result of proactive and close management of the Council's cash-flows (enabling delays to borrowing being taken) and despite the challenges faced with investment income and maintaining our low risk strategy.
- 7.4 There were no opportunities to further reduce the cost of our borrowing via rescheduling during the year.
- 7.5 The results (interest payable) for the year can be summarised as follows:

	Fixed Rate Debt	Market Debt	Variable Rate Debt	Total
Total Interest £M	5.257	4.371	0.004	9.632
Average Debt £M	114.046	87.500	0.793	202.339
Average Interest %	4.61%	5.00%	0.53%	4.76%

- 7.6 Members will also recall the previously reported position with regard to the accounting arrangements and treatment of LOBO's (Lender Option / Borrower Option). These loan instruments have enabled the Council to realise significant short-term and further ongoing reductions in its capital charges. These savings have been invested into key service improvements and the Treasury Management Reserve, which have helped not only to reduce risk around future financial market changes, but also as pump priming to produce more efficient and effective ongoing front line services for the taxpayer.

8.0 ESTIMATED AND ACTUAL TREASURY POSITION, PRUDENTIAL AND TREASURY INDICATORS

- 8.1 During the financial year 2012/13, the Council operated within its limits set out in the Prudential Code report approved in March 2012. Details of limits and actual performance are as follows:

		2012/13 Actual
Capital Expenditure 12/13		81.366M
Capital Financing Requirement (CFR) as at 31 st March 2013		356.333M

Limit / Indicator	2012/13 Limit / Indicator	2012/13 Actual
Authorised Limit (£) (Limit beyond which borrowing is prohibited)	304.802M	235.241M (at highest point in year)
Operational Boundary (£) (Indicator to ensure Authorised Limit not breached)	246.091M	226.056M (at year end)
External Debt	217.441M	197.450M
Other Long Term Liabilities	<u>0.800M</u>	<u>0.829M</u>
Sub total	218.241M	198.279M
Other : PFI and Finance Lease	<u>27.777M</u>	<u>27.777M</u>
Borrowing + Other Long Term Liabilities	246.018M	226.056M
Ratio of Financing Costs to Net Revenue Stream	5.97%	6.09%
Limit on Fixed Interest Rates	55% - 125%	62%
Limit on Variable Interest Rates	-25% - 45%	38%
Funds invested for greater than 1 year	£15M	£1m (refer to section 11)
LOBO Limit	£100M / 45% of debt portfolio	£85.5M / 38% of debt portfolio
Maturity Structure of Fixed Rate Debt	Under 12 mths 0-60% 12 mths – 2 yrs 0-60% 2-5 years 0-60% 5-10 years 0-70% 10-20 years 0-90% 20-30 years 0-90% 30-40 years 0-90% 40-50 years 0-90%	Under 12 mths 35% 12 mths – 2 yrs 0% 2-5 years 10% 5-10 years 0% 10-20 years 12% 20-30 years 0% 30-40 years 32% 40-50 years 11%

9.0 INVESTMENT STRATEGY

- 9.1 The Council manages its investments in-house, investing in line with the Council's approved lender criteria as approved by Council on the 21st March 2012. Investment policy is governed by Welsh Government guidance.
- 9.2 Members will recall that following the onset of the unprecedented national and international economic crisis in 2008, all of this Council's cash flows are currently being invested in the Debt Management Account Deposit Facility and other Government backed public sector bodies, in line with the aforementioned approved strategy. This low risk strategy was formed balancing risk and return. It is acknowledged that low risk investment strategies result in lower than benchmark investment returns.
- 9.3 I have kept this under constant review subsequently with a view to returning to market investment activity at an appropriate time. To date, the Council has not returned to market investments but has set up a number of AAA rated money market funds to provide further diversification options when the opportunity does arise. These accounts have not been used during 2012/13. Members will be kept informed of any changes as part of the Council's quarterly performance reports.
- 9.4 During the year, the Council has complied with the approved strategy and there have been no liquidity difficulties.
- 9.5 During 2012/13, the Council has not invested funds for longer than 364 days.

10.0 INVESTMENT ACTIVITY AND RESULTS

- 10.1 The following table shows the overall result of the investment activities undertaken by the Council:

	Interest Received	Average Cash Balance	Return on Investments	Benchmark Return
	£M	£M	%	%
Cash Balances	0.122	41.804	0.29	0.39

The benchmark for Local Authority internally managed funds is the average 7-day LIBID rate.

- 10.2 Despite our low risk strategy and lower than benchmark return on investments, we have managed to be within budget for overall capital charges (refer to para 7.3). The Economic Background section of this report set out the continuing difficulties in economic conditions during

this period. As a result of these conditions and our low risk strategy, interest rates remain low impacting adversely, but not unexpectedly, on investment returns.

- 10.3 The failure of the Icelandic banking system in October 2008 had a major impact on local authority investments across the UK. Over 100 local authorities had deposits of almost £1bn with these institutions.
- 10.4 Members will be aware that the Council has £3.0M invested with Heritable Bank Plc (in administration). On the 27th July 2012 the administrators issued their latest report to creditors which reaffirmed their estimated likely return to creditors, based on the progress of the administration to date and predicted future performance, at between 86 and 90 pence in the pound (base case return). To date, the total dividend payments received amount to £2.3M, with notification received that the next dividend payment is to be declared in August 2013. In line with Local Authority Accounting Panel Bulletin 82, the investment has been “impaired” based on an assumed 88% recovery.

11.0 LOCAL AUTHORITY MORTGAGE SCHEME (LAMS)

- 11.1 As approved by Council on 4th July, during September 2012, the Council launched the Local Authority Mortgage Scheme which supports First Time Buyers in purchasing a home. The scheme is facilitated by Lloyds Bank and allows First Time buyers to access 95% loan to value mortgages on terms similar to 75% loan to value mortgages. The bank is able to offer such loans where the Council guarantees the loan up to 20% of the value of the property. It is a requirement of the scheme that the Council places a deposit with the bank for the length of the indemnity. Therefore the Council has a deposit of £1m with Lloyds for 5 years.

12.0 CONCLUSION

- 12.1 The last financial year has been a further extremely challenging year for Treasury Management and this report highlights for Members that Treasury Management activities have operated effectively and within budgetary and prudential limits.

LOCAL GOVERNMENT ACT 1972

AS AMENDED BY

THE LOCAL GOVERNMENT (ACCESS TO INFORMATION) ACT 1985

RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL

COUNCIL

24 JULY 2013

REPORT OF THE GROUP DIRECTOR, CORPORATE SERVICES

Background Papers

2012/13 ANNUAL TREASURY MANAGEMENT REVIEW

Officer to Contact: Mr.S.Merritt – Tel. 01443 424088