AUDIT COMMITTEE – 15 FEBRUARY 2013

Title of paper:	**TREASURY MANAGEMENT 2012/13 – HALF YEARLY UPDATE**	
Director(s)/ Corporate Director(s):	Carole Mills Deputy Chief Executive & Corporate Director, Resources	**Wards affected: All**
Report author(s) and contact details:	Jeff Abbott, Head of Corporate and Strategic Finance Tel: 0115 8763648 E-mail: jeff.abbott@nottinghamcity.gov.uk	
Other colleagues who have provided input:	Members of Treasury Management Panel: Tony Kirkham, Director of Strategic Finance Geoff Walker, Strategic Finance Manager Barry Dryden, Senior Finance Manager Peter Guest, Treasury Management Officer	

Relevant Council Plan Strategic Priority: (you must mark ✓ in the relevant boxes below)	
World Class Nottingham	✓
Work in Nottingham	✓
Safer Nottingham	✓
Neighbourhood Nottingham	✓
Family Nottingham	✓
Healthy Nottingham	✓
Leading Nottingham	✓

Summary of issues (including benefits to citizens/service users):

This report sets out treasury management actions and performance from 1 April 2012 to 30 September 2012.

Recommendation(s):

1 To note the treasury management actions taken in 2011/12 to date, specifically that:

- No new long-term borrowing or debt rescheduling had been undertaken to 30 September 2012
- The average return on investments to 30 September 2012 was 0.807%
- Between 1 April and 30 September, daily cash flow performance was above target at 98.5%

1. BACKGROUND

Treasury management is the management of a local authority's cash flows, borrowings and investments, together with the management of the associated risks and the pursuit of the optimum performance or return consistent with those risks. Since 1 April 2004 councils have been required to have regard to the Prudential Code. The Code requires treasury management to be carried out in accordance with good professional practice. The City Council retains external advisors to assist with this activity.

Appendix 1 (the Executive Board report on this subject of 18 December 2012) provides details of treasury management activity to 30 September 2012.

2. REASONS FOR RECOMMENDATIONS (INCLUDING OUTCOMES OF CONSULTATION)

The Code requires authorities to nominate a body within the organisation to be responsible for scrutiny of treasury management activity. It is considered that the City Council's Audit Committee is the most appropriate body for this function. In undertaking this, the Audit Committee will be responsible for the effective scrutiny of treasury management policies and practices.

Under the Code, the annual Treasury Management Strategy is considered by a designated scrutiny body (Audit Committee) and approved by a full meeting of Nottingham City Council before the beginning of the financial year to which it applies. A half-yearly report is also a requirement of the Code, with any changes to the strategy required to be approved by a full Council meeting.

3. OTHER OPTIONS CONSIDERED IN MAKING RECOMMENDATIONS

Options for management of the Council's debt and investment portfolio are continually reviewed. The overall aim is to minimise the net revenue costs of our debt whilst maintaining an even debt profile in future years, and to maximise investment returns within stated security and liquidity guidelines.

4. FINANCIAL IMPLICATIONS (INCLUDING VALUE FOR MONEY/VAT)

The financial implications are shown in **Appendix 1, section 5.**

5. RISK MANAGEMENT ISSUES (INCLUDING LEGAL IMPLICATIONS AND CRIME AND DISORDER ACT IMPLICATIONS)

Risk management plays a fundamental role in treasury activities, due to the value of transactions involved. The management of specific treasury management risks is set out in the Manual of Treasury Management Practices and Procedures and a risk register is maintained for the treasury function.

6. EQUALITY IMPACT ASSESSMENT

Has the equality impact been assessed?

Not needed (report does not contain proposals or financial decisions)	✓
No	☐
Yes – Equality Impact Assessment attached	☐

7. LIST OF BACKGROUND PAPERS OTHER THAN PUBLISHED WORKS OR THOSE DISCLOSING CONFIDENTIAL OR EXEMPT INFORMATION

None

8. PUBLISHED DOCUMENTS REFERRED TO IN COMPILING THIS REPORT

Treasury Management in the Public Services, Code of Practice 2009 – CIPFA

APPENDIX 1

EXECUTIVE BOARD – 18 DECEMBER 2012

Subject:	**TREASURY MANAGEMENT 2012/13 – HALF YEARLY UPDATE**
Corporate Director(s)/ Director(s):	Tony Kirkham Director of Strategic Finance
Portfolio Holder(s):	Councillor Graham Chapman, Portfolio Holder for Resources, Economic Development and Reputation
Report author and contact details:	Jeff Abbott, Head of Corporate and Strategic Finance Tel: 0115 8763648 E-mail: jeff.abbott@nottinghamcity.gov.uk

Key Decision ☐**Yes** ε **No**

Reasons: Expenditure ☐ Income ☐ Savings ☐ of £1,000,000 or more taking account of the overall impact of the decision	Revenue ☐ Capital ☐
Significant in terms of its effects on communities living or working in an area consisting of two or more wards in the City	☐ Yes No ☐

Relevant Council Plan Strategic Priority:		**Wards affected:** ALL
World Class Nottingham	ε	
Work in Nottingham	ε	
Safer Nottingham	ε	
Neighbourhood Nottingham	ε	**Date of consultation with Portfolio Holder(s):** Throughout the financial year to date
Family Nottingham	ε	
Healthy Nottingham	ε	
Leading Nottingham	ε	

Summary of issues (including benefits to citizens/service users):

This report sets out details of treasury management actions and performance from 1 April 2012 to 30 September 2012.

Recommendation(s):

To note the treasury management actions taken in 2011/12 to date, specifically that:

- No new long-term borrowing or debt rescheduling had been undertaken to 30 September 2012
- The average return on investments to 30 September 2012 was 0.807%
- Between 1 April and 30 September, daily cash flow performance was above target at 98.5%

1 BACKGROUND

1.1 Treasury management is the management of the local authority's cash flows, borrowings and investments, together with the management of the associated risks and the pursuit of the optimum performance or return consistent with those risks. Since 1 April 2004 local authorities have been required to have regard to the Prudential Code. The Code requires treasury management to be carried out in accordance with good professional practice. The Council retains external advisors to assist with this activity.

1.2 In respect of external investments, the Council is also required to ensure that CLG guidance is followed, with priorities being:

- security of the invested capital
- liquidity of the invested capital and
- Commensurate with security and liquidity, an optimum return on those investments.

1.3 The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Treasury management risks are identified in the Council's approved Treasury Management Practices. The main risks to the Council's treasury activities are:

- liquidity risk (inadequate cash resources)
- market or interest rate risk (fluctuations in interest rate levels and thereby in the revenue impacts of loans and investments)
- inflation risks (exposure to inflation)
- credit and counterparty risk (security of investments)
- refinancing risks (impact of debt maturing in future years)
- Legal and regulatory risk (i.e. non-compliance with statutory and regulatory requirements, risk of fraud).

2 REASONS FOR RECOMMENDATIONS (INCLUDING OUTCOMES OF CONSULTATION)

To ensure that councillors are kept informed of the actions taken by the Chief Finance Officer (CFO) under delegated authority. The current Treasury Management Code of Practice, adopted by the Council, requires the CFO to submit a minimum of three reports on treasury management each year; a policy and strategy statement for the ensuing financial year, a 6-monthly progress report and an outturn report. It is also a requirement of the Code that the reports be considered by relevant scrutiny or executive committees, and that a meeting of the City Council approve any treasury management strategy decisions.

3 TREASURY MANAGEMENT ACTIVITY TO 30 SEPTEMBER 2012

3.1 <u>2012/13 strategy</u>
The overall Treasury Management Strategy for 2012/13 was approved by the City Council on 5 March 2012. Amendments to the investment strategy were considered by Executive Board and Audit Committee (on 18 and 21 September respectively and approved by the S151 officer, under delegated authority).

Table 1 shows the actions taken as at 30 September 2012 against each of the main four elements of the strategy:

TABLE 1: TREASURY MANAGEMENT ACTIONS	
Strategy 2012/13	**Actions to 30 September 2012**
New borrowing – to raise up to £53.8m to finance new capital expenditure in the year and replace maturing long-term debt.	To 30 September, no new debt had been raised. (*see 3.3*)
Debt rescheduling – to give consideration to any debt rescheduling or repayment opportunities which enable revenue savings to be generated in the year.	To 30 September, no debt rescheduling had taken place (*see 3.4*)
Investments – to ensure the security of funds invested through the application of a restricted counterparty list and maximum periods of investment. Within those confines, to maximise the return on investments.	The average return on investments from 1 April to 30 September 2012 was 0.807%. The benchmark average 7-day LIBID rate for the same period was 0.537%. (The 2012/13 budget assumed an average return of 1.050% for the period). (*see 3.5)*
Daily cash management – to maintain an overnight cash balance between £0.3m overdrawn and £0.15m in-hand every day. The 2012/13 target is to exceed 98.9% (2011/12 performance)	Between 1 April and 30 September 2012 performance was just below target, at 98.5%.

3.2 Interest rates during 2012/13

The Bank of England Base Interest Rate of 0.50% has been unchanged in 2012/13. With the economic recovery in the UK developing only slowly, it is expected that the base rate will remain at its current level for the next two years at least.

Short-term interest rates have been kept low by a combination of the retention of the UK's AAA credit rating, which has attracted a large inflow of investors into safe haven UK gilts and the Government's Quantitative Easing and Funding for Lending programmes, designed to increase the liquidity in financial markets. As a consequence, interest rates from 1 month to a year have fallen significantly since the beginning of the financial year.

Longer-term interest rates have also been affected, to a lesser extent, by investors seeking a safe haven, with rates declining steadily since the start of the financial year. **Table 2** overleaf shows a range of interest rates over the period from 1 April to 30 September:

TABLE 2: INTEREST RATES 2012/13								
Date	**Base Rate %**	**1 month**	**3 month**	**6 month**	**1 year**	**5 years**	**20 years**	**50 years**
		%						
1 Apr	0.50	0.67	1.03	1.36	1.87	2.10	4.23	4.44
1 May	0.50	0.66	1.02	1.35	1.87	2.11	4.14	4.38
1 Jun	0.50	0.63	1.00	1.33	1.85	1.83	3.68	4.04
1 Jul	0.50	0.58	0.87	1.18	1.69	1.68	3.77	4.15
1 Aug	0.50	0.50	0.69	0.97	1.47	1.60	3.61	4.07
1 Sep	0.50	0.47	0.63	0.87	1.32	1.59	3.61	4.10
1 Oct	0.50	0.46	0.52	0.74	1.11	1.72	3.76	4.18

3.3 Long-term borrowing

The continuing low return on short-term investments, coupled with a more benign forecast for long term interest rates, has led to the deferral in the raising of long-term borrowing in the last 2 financial years, with a combination of internal cash balances and short-term borrowing being used as a (temporary) source of finance. This approach has continued in the current financial year, with no new long term borrowing raised to 30 September.

3.4 Debt rescheduling

The opportunities for debt rescheduling during 2012/13 have been limited. Low interest rates mean that the repayment of existing long-term debt incurs financial penalties that mitigate against such action.

3.5 Investments

The City Council's cash investments represent reserves and provisions held within the balance sheet plus surplus working capital. As at 30 September 2012, all investments were managed in-house. The 2012/13 budget assumed an average cash surplus of £123.0m during the year. The actual average cash balance to 30 September was £145.7m, as a result of the receipt of a number of grant payments in advance of required expenditure.

The average rate of interest earned on all investments to 30 September was 0.807%. The original budget assumed a return of 1.050% for the same period. The fall in return reflects continuing lower short term interest rates as a result of the large-scale injection of liquidity into capital markets by the Government's Monetary Policy Committee, as they seek to stimulate growth in the UK economy. For comparison purposes, the benchmark 7-day LIBID interest rate for the same period was 0.537%.

3.6 2012/13 Investment strategy

The 2011/12 approved investment strategy allows for investments with the following counterparties; the Government's Debt Management Office, other local authorities, UK and overseas banks meeting the required criteria in respect of credit ratings etc, Money Market Funds (pooled, short maturity, high quality investment vehicles offering instant access), UK gilts and treasury bills and Supranational Bonds. The adoption of specific counterparties is based on a wide range of criteria, including credit ratings, credit default swap rates, government support mechanisms and parent bank support. Maximum sums and periods of investment are set for individual counterparties.

During the year, monitoring of the financial position of all counterparties is undertaken by treasury management colleagues and retained advisors. This process considers individual credit ratings, credit default swap prices, share prices, changes in sovereign state credit ratings and more general developments in financial markets and the global economy. This then informs any decisions to revise the investment strategy. Where considered necessary, individual counterparties may be suspended from the approved list, or the maximum period for investment reduced.

In September, following the suspension of a number of European and other banks and a reduction in the maximum investment period for others, proposed changes to the investment strategy were submitted to Executive Board and Audit Committee. In the absence of a City Council meeting until December, the changes were approved by the S 151 officer, under delegated authority. The effect of the changes was to:

- re-instate the Royal Bank of Scotland (a UK bank considered systemically important to the UK financial system) on the eligible counterparty list
- increase the maximum investment sum for eligible UK banks to £25m, reflecting the increased size of the overall investment portfolio, and
- Increase the maximum investment sum for eligible non-UK banks to £10m, again reflecting the size of the portfolio.

3.7 Icelandic Bank deposits – update

The City Council had £41.6m invested over three Icelandic banks, which collapsed in October 2008. These banks have continued to pass through an administration process to determine the level of payments to be made to the banks' creditors. The latest position in respect of deposits with each bank is:

a) Heritable Bank (original deposit £15.6m) – the administrators continue to realise the assets of the bank and make stage payments to creditors. To date, repayments of principal and interest totalling £11.9m have been received, representing around 75% of the original investment. It is currently estimated that the final sum recovered will be c 88% of the original deposit.

b) Landsbanki Bank (£15m) – repayments in sterling totalling £7.4m have been received. It is considered that 100% of the sum deposited will be recovered in time, although the last stage payment is not scheduled until 2018, and the final amount is subject to currency exchange rate fluctuations.

c) Glitnir Bank (£11m) – the administrators have made repayment to all priority creditors, including the City Council, in full settlement of the accepted claims. However, approximately 21% of this sum has been paid in Icelandic Krone (ISK). Because of ongoing currency restrictions in Iceland, this sum is currently retained in an interest-bearing account with the Central Bank of Iceland, pending resolution of the currency release issues.

4 OTHER OPTIONS CONSIDERED IN MAKING RECOMMENDATIONS

Options for management of the City Council's debt and investment portfolio are continually reviewed. The overall aim is to minimise the net revenue costs of our debt whilst maintaining an even debt profile in future years, and to maximise investment returns within stated security and liquidity guidelines.

5 FINANCIAL IMPLICATIONS (INCLUDING VALUE FOR MONEY)

Treasury management payments comprise interest charges and receipts and provision for repayment of debt. A proportion of the City Council's debt relates to capital expenditure on council housing and this is charged to the HRA. The remaining costs are included within the treasury management section of the General Fund budget. **Table 3** sets out the original budget for 2012/13, with the forecast outturn for the year also shown.

TABLE 3: TREASURY MANAGEMENT REVENUE BUDGET		
DESCRIPTION	**Budget 2012/13 £m**	**Forecast Outturn 2012/13 £m**
External interest	30.277	29.712
Debt repayment provision	31.426	27.692
Prudential borrowing recharge	(0.562)	(0.562)
Investment interest	(1.350)	(1.350)
Other interest	(0.151)	(0.151)
Less: HRA interest charge	(12.781)	(12.781)
Transfer to/(from) TM reserve	-	-
Net General Fund position	**46.859**	**42.560**

The forecast outturn for 2012/13 reflects revenue savings in the year (interest and debt repayment provision) arising from capital financing decisions in 2011/12 and the net result of the Government's Housing Revenue Account self-financing exercise undertaken in March 2012. These savings are also included in the Revenue and Capital budget review (Period 7) included elsewhere on this agenda.

Full details of the 2012/13 outturn, together with budget estimates for the next 3 financial years will be submitted to Executive Board with the 2013/14 treasury management strategy report, in February 2013.

6 RISK MANAGEMENT ISSUES (INCLUDING LEGAL IMPLICATIONS, CRIME AND DISORDER ACT IMPLICATIONS)

Risk management plays a fundamental role in treasury activities, due to the value and nature of transactions involved. The management of specific treasury management risks is set out in the Manual of Treasury Management Practices and Procedures and a risk register is prepared for the treasury function.

7 EQUALITY IMPACT ASSESSMENT (EIA)

Has the equality impact been assessed?

(a) not needed (report does not contain proposals for new or changing policies, services or functions, financial decisions or decisions about implementation of policies development outside the Council) ε

(b) No ☐

(c) Yes – Equality Impact Assessment attached ☐

8 LIST OF BACKGROUND PAPERS OTHER THAN PUBLISHED WORKS OR THOSE DISCLOSING CONFIDENTIAL OR EXEMPT INFORMATION

None

9 PUBLISHED DOCUMENTS REFERRED TO IN COMPILING THIS REPORT

Treasury Management in the Public Services, Code of Practice 2009 – CIPFA

10 OTHER COLLEAGUES WHO HAVE PROVIDED INPUT

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