EXECUTIVE BOARD – 19 NOVEMBER 2013

<table>
<tr><td>Subject:</td><td colspan="3">TREASURY MANAGEMENT 2013/14 HALF YEARLY UPDATE</td></tr>
<tr><td>Corporate Director(s)/ Director(s):</td><td colspan="3">Carole Mills, Deputy Chief Executive/Corporate Director for Resources</td></tr>
<tr><td>Portfolio Holder(s):</td><td colspan="3">Councillor Graham Chapman, Deputy Leader/Portfolio Holder for Resources and Neighbourhood Regeneration</td></tr>
<tr><td>Report author and contact details:</td><td colspan="3">Tony Kirkham, Director of Strategic Finance
0115 8764157
tony.kirkham@nottinghamcity.gov.uk</td></tr>
<tr><td colspan="4">Key Decision ☐ Yes ☒ No</td></tr>
<tr><td colspan="3">Reasons: Expenditure ☐ Income ☐ Savings ☐ of £1,000,000 or more taking account of the overall impact of the decision</td><td>Revenue ☐ Capital ☐</td></tr>
<tr><td colspan="3">Significant in terms of its effects on communities living or working in an area consisting of two or more wards in the City</td><td>☐ Yes No ☐</td></tr>
<tr><td colspan="2">Subject to call-in ☒ Yes No ☐</td><td colspan="2">Total value of the decision: Nil</td></tr>
<tr><td colspan="2">Relevant Council Plan Strategic Priority:</td><td colspan="2" rowspan="4">Wards affected:
All</td></tr>
<tr><td>World Class Nottingham</td><td>☒</td></tr>
<tr><td>Work in Nottingham</td><td>☒</td></tr>
<tr><td>Safer Nottingham</td><td>☒</td></tr>
<tr><td>Neighbourhood Nottingham</td><td>☒</td><td colspan="2" rowspan="4">Date of consultation with Portfolio Holder(s):
Throughout the financial year to date</td></tr>
<tr><td>Family Nottingham</td><td>☒</td></tr>
<tr><td>Healthy Nottingham</td><td>☒</td></tr>
<tr><td>Leading Nottingham</td><td>☒</td></tr>
<tr><td colspan="4">Summary of issues (including benefits to citizens/service users):
This report sets out details of treasury management actions and performance from 1 April 2013 to 30 September 2013.</td></tr>
<tr><td colspan="4">Recommendation(s):</td></tr>
<tr><td colspan="4">1 To note the treasury management actions taken in 2013/14 to date, specifically that:
• no new long-term borrowing or debt rescheduling had been undertaken to 30 September 2013;
• the average return on investments to 30 September 2013 was 0.667%;
• between 1 April and 30 September daily cash flow performance was above target, at 100%.</td></tr>
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1 BACKGROUND (INCLUDING OUTCOMES OF CONSULTATION)

1.1 Treasury management is defined as the management of an organisation'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. This Code requires treasury management to be carried out in accordance with good professional practice. The Council retains external advisors to support this activity.

1.2 In respect of external investments, the Council is also required to ensure that Communities and Local Government (CLG) department guidance is followed, with the priorities being, in order:

- 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 successful identification, monitoring and control of risk are the prime criteria by which the effectiveness of our treasury management activities is measured. Treasury management risks are identified in the Treasury Management Practices document. 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

2.1 To ensure that Councillors are kept informed of the actions taken by the Chief Finance Officer (CFO) under delegated authority. The currently adopted Treasury Management Code of Practice requires the CFO to submit at least 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 after the end of the financial year. The Code also requires that the reports be considered by relevant scrutiny or executive committees, and that the City Council approves any treasury management strategy decisions.

3 OTHER OPTIONS CONSIDERED IN MAKING RECOMMENDATIONS

3.1 No other options were considered as the report is required by the Treasury Management Code of Practice.

4 TREASURY MANAGEMENT ACTIVITY TO 30 SEPTEMBER 2013

4.1 2013/14 Strategy

The overall Treasury Management Strategy for 2013/14 was approved by the City Council on 4 March 2013. **Table 1** summarises the actions taken to 30 September 2013 against each of the main four elements of that strategy:

TABLE 1: TREASURY MANAGEMENT ACTIONS	
Strategy 2013/14	**Actions to 30 September 2013**
New borrowing – to raise up to £74.2m to finance new capital expenditure in the year and replace maturing long-term debt.	To 30 September, no new long-term borrowing had taken place. (see 4.3*)*
Debt rescheduling – to consider 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 4.4)
Investments – to ensure the security of funds invested through the application of a restricted counterparty list and the imposition of limits on the period and levels of individual investments. Within those confines, to maximise the return on investments.	The average return on investments from 1 April to 30 September 2013 was 0.667%. The benchmark average 7-day London Inter-Bank Bid (LIBID) rate for the same period was 0.540%. The 2013/14 budget assumed an average return of 0.783% for the period. (see 4.5)
Daily cash management – to maintain an overnight cash balance between £0.3m overdrawn and £0.15m in-hand, for every day. The 2013/14 target is to exceed 98.83% (2012/13 performance)	Between 1 April and 30 September 2013 performance was above target, at 100.0%.

4.2 Interest rates during 2013/14

The Bank of England Base Interest Rate of 0.50% has been so far unchanged in 2013. Although the UK has shown some positive signs of economic recovery during the year, this recovery is developing only slowly and it is currently expected that the base rate will remain at its present level until 2015 at the earliest.

Short-term interest rates have continued to be kept low by a combination of the Government's Quantitative Easing and Funding for Lending programmes, designed to increase the liquidity in financial markets. The appointment of a new Bank of England Governor, and the introduction of 'forward' guidance from the Monetary Policy Committee has reinforced the view that increases to base interest rates will only begin when the Unemployment Rate falls to 7.00%. This expectation is likely to keep short-term interest rates at current levels for the remainder of the current financial year at least.

Longer-term interest rates have increased in 2013 across all periods, partly as a general market correction and partly on the expectation that the US Federal Reserve would start to taper and remove its own Quantitative Easing Programme. **Table 2** shows actual interest rates for the half-year from 1 April:

TABLE 2: INTEREST RATES 2013/14								
Date	**Base Rate %**	**1 month**	**3 month**	**6 month**	**1 year**	**5 year**	**20 year**	**50 year**
		%						
1 Apr	0.50	0.50	0.51	0.61	1.11	1.74	3.87	4.21
1 May	0.50	0.50	0.51	0.60	1.17	1.75	3.76	4.09
1 Jun	0.50	0.50	0.51	0.59	1.27	2.03	4.06	4.39
1 Jul	0.50	0.51	0.52	0.60	1.24	2.40	4.35	4.58
1 Aug	0.50	0.55	0.53	0.61	1.20	2.19	4.27	4.47
1 Sep	0.50	0.51	0.53	0.61	1.31	2.60	4.50	4.59
1 Oct	0.50	0.51	0.53	0.61	1.31	2.51	4.33	4.45

4.3 Borrowing

The continuing low return on short-term investments, coupled with the ready availability of cheap short-term borrowing, 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 debt being used as a preferred source of finance. Although long-term borrowing costs have started to increase, the margins between short and long-term interest rates remains an important influence on the Council's borrowing strategy and no new long-term borrowing was raised to 30 September. Existing cash surpluses have been used to fund maturing debt in the year. **Table 3** summarises the Council's outstanding external debt at 30 September 2013:

TABLE 3: DEBT PORTFOLIO		
	30 SEP 2013	
DEBT	**£m**	**%**
PWLB borrowing	655.5	3.953
Market loans	51.3	4.287
Local bonds	0.5	2.070
Temporary borrowing	16.2	0.408
TOTAL DEBT	**723.5**	**3.891**

4.4 Debt rescheduling

The penalties (premia) for the early repayment of Public Works Loan Board (PWLB) debt, which constitutes over 90% of the Council's existing long-term borrowing, have remained prohibitively high. Therefore, no opportunities for debt rescheduling arose in the first half of 2013.

4.5 Investments

The 2013/14 approved investment strategy allows for investments with the following counterparties; the UK Government's Debt Management Office, UK Government Gilts and Treasury Bills, other local authorities, UK and overseas banks meeting the required investment criteria, Money Market Funds (pooled, short maturity, high quality investment vehicles offering instant access) 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 and credit default swap prices, plus 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 amount or period of investment reduced.

The Council's cash investments represent reserves and provisions held within the balance sheet, plus surplus working capital. During 2013 to date, all investments have been managed in-house. The original 2013/14 budget assumed an average cash surplus of £232.5m during the year. The actual average cash balance to 30 September was £251.7m, largely 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 0.667%. The original budget assumed a return of 0.783% 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. In comparison, the benchmark 7-day LIBID interest rate for the same period was 0.540%.

The impact of the two variances above is broadly neutral, with the latest forecast for investment income in 2013/14 showing only a small variance from the original estimate of £1.050m.

Appendix A provides details of the Council's external investments of £195m at 30 September 2013, analysed between investment type and individual counterparties.

4.6 <u>Icelandic Bank deposits – update</u>

The City Council had £41.6m invested over three Icelandic banks, when the Icelandic banking system collapsed in October 2008, forcing all three banks into administration. Since then, 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 the Council's deposits with each bank is:

a) Heritable Bank (original deposit £15.6m) – the administrators have continued to realise the assets of the bank and make stage payments to creditors. To date, repayments of principal and interest totalling £14.982m have been received, around 94% of the original investment. The likelihood of further repayments is dependant on an ongoing court case between Heritable Bank and its parent Landsbanki Bank.

b) Landsbanki Bank (£15m) – repayments in sterling totalling £8.197m have been received to date. It is currently forecasted that 100% of the sum deposited will be repaid by the administrators, although the final instalment payment is not currently scheduled before 2018, and the actual amount received is be subject to a number of variables including exchange rate fluctuations and the release of any payments made in Icelandic Krone (ISK) – see Glitnir below.

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 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.

5 FINANCIAL IMPLICATIONS (INCLUDING VALUE FOR MONEY/VAT)

5.1 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 Housing Revenue Account (HRA). The remaining costs are included within the treasury management section of the General Fund budget. **Table 4** sets out the current budget for 2013/14 compared with the actual for 2012/13:

TABLE 4 – GENERAL FUND (TREASURY MANAGEMENT)		
DESCRIPTION	**Actual 2012/13 £m**	**Budget 2013/14 £m**
External interest	29.079	30.929
Debt repayment provision	29.976	32.583
Prudential borrowing recharge	(0.566)	(0.516)
Investment interest	(1.060)	(1.050)
Other interest	(0.162)	(0.132)
Less: HRA interest element	(12.385)	(11.605)
Transfer to/(from) TM reserve	1.726	-
Net General Fund position	**46.608**	**50.209**

5.2 An estimated outturn for 2013/14, together with budgets for 2014/15 through to 2015/16 will be submitted with the 2014/15 treasury management strategy, in February 2014.

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

6.1 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 SOCIAL VALUE CONSIDERATIONS

7.1 Not applicable.

8 REGARD TO THE NHS CONSTITUTION

8.1 Not applicable.

9 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 outsi the Council)	☒
(b)	No	☐
(c)	Yes – Equality Impact Assessment attached	☐

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

10.1 None

11 PUBLISHED DOCUMENTS REFERRED TO IN COMPILING THIS REPORT

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

12 OTHER COLLEAGUES WHO HAVE PROVIDED INPUT

Pete Guest, Treasury Management Officer
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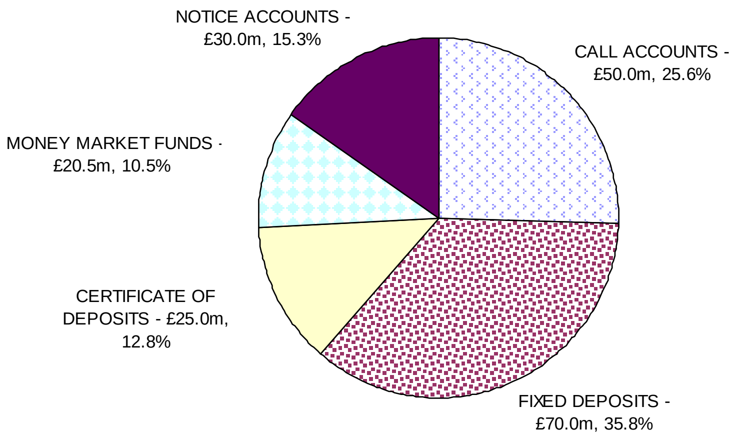
APPENDIX A

Type of Investment at 30 September 2013



Investment and Fitch credit ratings at 30 September 2013