Nottinghamshire and City of Nottingham
Fire and Rescue Authority
Finance and Resources Committee

TREASURY MANAGEMENT ANNUAL REPORT 2008/09

Report of the Treasurer to the Fire Authority

Agenda Item No:

Date: 09 October 2009

Purpose of Report:

To give Members a comprehensive picture of all Treasury Management policies, plans, activities and results for the financial year 2008/09.

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1. BACKGROUND

1.1 The Local Government Act 2003 requires the Authority to set out its treasury strategy for borrowing and to prepare an annual investment strategy; this sets out the Authority's policies for managing its investments and for giving priority to the security and liquidity of those investments.

1.2 The Authority has adopted the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management and fully complies with its requirements. The primary requirements of the Code are the:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Authority's treasury management activities

- Creation and maintenance of Treasury Management Practices which set out the manner in which the Authority will seek to achieve those policies and objectives.

- Receipt by the Authority of an annual strategy report for the year ahead and an annual review report of the previous year.

- Delegation by the Authority of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

1.3 Treasury management in this context is defined as:

"The management of the Authority's cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks. "

2. REPORT

TREASURY POSITION

2.1 The Authority's debt and investment position at the beginning and the end of the year was as follows:

	31 March 2009		31 March 2008	
	Principal £m	Average rate %	Principal £m	Average rate %
Fixed rate borrowing: PWLB				
Maturing:				
Within 5 years	5.289		0.274	
5 to 10 years	2.376		0.357	
10 – 15 years	0.199		0.283	
Over 15 years	4.900		4.900	

Total PWLB Debt	12.764	3.985%	5.814	4.337%
Fixed rate borrowing:				
Dexia Bank (maturing over 15 years)	4.000	4.13%	4.000	4.13%
Nottinghamshire County Council (less than 1 year)	1.500	1.25%	0	0
Investments (short term)	2.656	3.458%	5.521	5.865%

OVERVIEW OF CAPITAL TRANSACTIONS

2.2 A report on proposed capital expenditure and capital financing plans was submitted to the Authority on 22 February 2008. Members approved this report and the plans set out within it.

2.3 Planned (plus slippage from 2007/08 and approved variations in the year) and actual capital expenditure for 2008/09 was as follows:

Capital Expenditure 2008/09	**Planned**	**Actual**
	£000's	**£000's**
Transport	3,594	2,206
Property	3,285	7,499
Information Technology & Communications Specialist Operational Equipment	830 30	326 0
Total	7,739	10,031

2.4 The overspend on the Property capital programme was mainly due to the delayed completion of the sale of Dunkirk Fire Station, which meant that the expected capital receipt was not received. The Transport underspend mainly related to fire appliances which are in the build stage and due to be completed in 2009/10. The ICT programme contained key projects which did start in the year, but which have not yet completed. Slippage has been carried forward and added to the 2009/10 Capital Programme.

2.5 The Authority's capital financing requirement is the sum of money, to be obtained from external sources, to fund capital expenditure. It excludes revenue funding used to finance capital and it also excludes capital receipts used to finance capital. The Authority's capital financing requirement at the beginning and the end of the year was as follows:

	£000's
Capital Financing Requirement at 31 March 2008	14,858
Capital Financing Requirement at 31 March 2009	24,170

2.6 During the year, the following sources of funding were used to finance capital expenditure:

	£000's
New borrowing	7,000
Capital Receipts	1,345
Total Financing of Capital Expenditure	8,345

THE ECONOMY

2.7 The financial year saw a significant downturn in the UK and global economic climate, with the UK entering a recession. The bank rate fell several times during the year from 5% at the start of the year to 0.5% by the end of March 2009.

2.8 On 15th September the US investment bank, Lehman Brothers filed for bankruptcy and this event caused a shock wave in world financial markets and threatened to completely destabilise them. On 7th October the Icelandic government took control of their banks and this was followed a few days later by the UK government injecting £37bn into three UK clearing banks: RBS, HBOS and Lloyds, as liquidity in the financial markets dried up.

2.9 Further Government support for the banking sector was announced on 19th January 2009. There was discussion in March about other measures that could be introduced to kick start lending and economic activity. These included quantitative easing by the Bank of England i.e. an injection of new money into the UK economy.

2.10 The financial year ended with markets still badly disrupted, the real economy suffering from a lack of credit, short to medium term interest rates at record lows and a great deal of uncertainty as to how or when recovery would take place.

2.11 The impact of this on the Authority is that falling interest rates have reduced the level of investment interest received in the latter half of the year although the Authority benefited to some extent from lower interest rates on borrowing. These effects can be seen in the table in paragraph 2.1 above.

BORROWING OUTTURN FOR 2008/09

2.12 The PWLB 45-50 year rate started the year at 4.43% and was then generally within a band of 4.3 - 4.6% until mid October when there was a spike up to 4.84% followed by a fall down to 3.86% in early December. Further spikes of 4.84% and 4.72% occurred in late January and early February with the year closing at 4.58%. It was not uncommon to see rates fluctuating by 40-50 basis points within a few weeks during this year.

2.13 The Authority, advised by Sector, made a decision to borrow from the PWLB to finance the capital programme during November. To balance the loan maturity of the total debt portfolio and in line with the Treasury Management Strategy, three loans were taken with relatively short maturity dates. The details are shown in the table below:

Term of Loan (years)	Amount	Maturity date	Interest rate
4	£2m	30/09/2012	3.46%
5	£3m	30/09/2013	3.71%
6	£2m	30/09/2014	3.93%

As a comparative performance indicator, the average PWLB maturity loan interest rate for 5 year loans during 2008/09 was just below 4%

2.14 Our performance against the prudential code indicators for the year was as follows:

Loan maturity profile			
Term of Loan	**Upper Limit**	**Lower Limit**	**Actual Performance**
Under 12 months	20%	0%	8.55%
12 months to 5 years	20%	0%	28.66%
5 years to 10 years	75%	0%	13.00%
Over 10 years	100%	25%	49.79%

2.15 The table above shows that in the “12 months to 5 years” maturity band the upper limit of 20% has been exceeded by almost 9%. This relates to £3m of the £7m of PWLB loans taken in November 2008. At the time of borrowing the loan fell within the “5 years to 10 years” maturity band, but by the end of March 2009 had moved into the “12 months to 5 years” band. This issue was considered at the time the Prudential Code for 2009/10 was being prepared, and the conclusion was that the higher level of debt maturing within 5 years did not pose a risk to the Authority, providing that this was balanced with longer term debt. As a result, the loan maturity upper limit for “12 months to 5 years” was amended to 30% in the Prudential Code for 2009/10.

2.16 The Authority set prudential limits for 2008/09 relating to the amount of indebtedness which could be sustained. These limits are the Operational Boundary, which reflects the Authority’s most likely total debt at any time in the year, and the Authorised Limit, which reflects the maximum total debt at any time in the year. The Authorised Limit allows headroom over the Operational Boundary to take account of the possible need to borrow short term to cover unusual cashflow movements.

2.17 The Operational Boundary for 2008/09 was £22.473m and the Authorised Limit for 2008/09 was £24.720m. The actual maximum amount of indebtedness during the year was £17.621m, which was well within both limits.

INVESTMENT OUTTURN FOR 2008/09

2.18 The Authority manages its investments in-house and invests with the institutions listed on its approved lending list. The Authority invests for a range of periods from overnight to up to one year, dependent on cash flows, its interest rate view and the interest rates on offer. Overnight investments and / or investments with a value of less than £1,000,000 can be difficult to place with institutions on the approved lending list or may attract relatively low rates of interest. In these situations surplus cash may be deposited either in the investment account with our bankers, Barclays Bank PLC or in an investment account (Base Plus Account) with the Bank of Scotland. During 2008/09, the Bank of Scotland's credit rating fell, causing it to be removed from the Authority's lending list. Consequently, surplus cash which has not been placed with other lending list institutions has only been invested with Barclays Bank.

2.19 The official bank rate was 5.0% at the start of the financial year and ended the year at 0.5%. The plummeting rates of interest had a significant impact on investment income earned, particularly in the second half of the year. During the autumn when the credit crunch kicked in and Icelandic banks failed, a number of institutions suffered falling credit ratings leading to concerns about the security of investments. Members of Policy and Strategy Committee received a Treasury Management Update report on 17 October 2008 and agreed a revised Treasury Management strategy, which included using cash resources to finance the capital programme in the short term, thereby reducing the amount available to invest with other institutions which might subsequently fail. It was also agreed that deposits could be made with the Government's Debt Management Office. The revised policies reduced the Authority's exposure to risk, but also had the consequence of reducing investment income, which was compounded by lower interest rates.

2.20 On 12 November 2008, a £2m investment was placed with the Bank of Ireland for 365 days after the Irish Government had confirmed that it would guarantee deposits placed with its banks. This was considered to be a secure investment at the time and continues to be, despite the fact that the Bank of Ireland's credit rating subsequently fell to the extent that it was removed from the Authority's lending list. The investment is earning interest at a rate of 4.56%, and this has helped significantly in achieving the investment income target of £220,000 for 2008/09. The actual amount of interest earned for the year was £213,578

2.21 Cashflow forecasts are prepared covering a period of 3 years and are checked and maintained on a daily basis. The aim is to ensure that there are sufficient funds in the Authority's bank account to pay all creditors as they fall due, whilst keeping the bank account balance to a minimum level and investing any surplus cash. As forecasts can sometimes be incorrect, for example if income receipts are unexpectedly delayed, the Authority has an approved overdraft limit of £200,000 and a prudential limit of £500,000 for the maximum overdraft. During 2008/09, the maximum amount overdrawn was £56k.

2.22 During the year the Authority maintained the policy of lending only to institutions on the approved lending list, with a temporary procedure put in place in October 2008 of only lending to UK and Irish institutions on the approved lending list, to reduce the risk of loss of capital. A variety of investments were made, with sums ranging from £251k to £3.5m and periods of investment ranging from overnight to 365 days.

2.23 The Authority set the following prudential limits for interest rate exposures in 2008/09:

Upper limit for variable rate interest exposures	30%
Upper limit for fixed rate interest exposures	100%

In 2008/09, 100% of investments were made at fixed rates of interest.

3. FINANCIAL IMPLICATIONS

The financial implications of this report are set out in full within the body of the report.

4. HUMAN RESOURCES AND LEARNING AND DEVELOPMENT IMPLICATIONS

There are no human resources or learning and development implications arising directly from this report.

5. EQUALITY IMPACT ASSESSMENT

There are no equalities issues arising directly from this report.

6. CRIME AND DISORDER IMPLICATIONS

There are no crime and disorder implications arising directly from this report.

7. LEGAL IMPLICATIONS

There are no legal implications arising directly from this report.

8. RISK MANAGEMENT IMPLICATIONS

The Prudential Code is a framework which sets out to quantify and minimise financial risk arising from the financing of capital, the investment of surplus funds and the maintenance of operating cash balances for the Authority. The favourable performance against the prudential targets demonstrates that these areas of operation are being managed effectively.

9. RECOMMENDATIONS

That Members note the contents of this report

10. BACKGROUND PAPERS FOR INSPECTION (OTHER THAN PUBLISHED DOCUMENTS)

None.

Peter Hurford
TREASURER TO THE FIRE AUTHORITY