

NORTH LINCOLNSHIRE COUNCIL

AUDIT SUB-COMMITTEE

QUARTERLY TREASURY MANAGEMENT AND STRATEGY REPORT 2011-12

1. OBJECT AND KEY POINTS IN THIS REPORT

- 1.1 To provide a regular review of the treasury strategy approved each year by council.
- 1.2 This is a report on treasury management performance between April 2011 and February 2012. The report explains how the strategy has been implemented to date, and the response to changing conditions in financial markets.
- 1.3 The report also provides an update on our Icelandic investments.

2. BACKGROUND INFORMATION

- 2.1 The **investment strategy for 2011/2012** aims to reduce risk by
 - Investing for shorter periods up to six months
 - Investing In UK institutions with high credit ratings or equivalent
 - Applying a maximum investment limit of £5m for most
 - Applying a maximum limit to financial groups rather than separate institutions
 - Deferring use of highly rated foreign banks for now.
- 2.2 The **borrowing strategy for 2011/2012** aims to
 - Suspend borrowing in the plan period for as long as is prudent
 - Track the differential between short-and long-term interest rates to determine when it is prudent to resume borrowing
 - Borrow only to support the capital programme
 - Maximize borrowing through the PWLB while this gives best value for money
 - Borrow for shorter periods if cash flow requires and
 - Consider debt rescheduling.

- 2.3 The council's budget was framed against the state of financial markets at that time and prospects for the year ahead. This included a Bank of England Base Rate of 0.5% since 5 March 2009. Most economists' expectations were that rates would increase to 1% during 2011/12, and to 1.5% in 2012/13. However, the governor of the Bank of England has now suggested that rates will stay low until 2013, with some forecasters predicting no change within the next three years.
- 2.4 The budget also projects an average cost of borrowing of 5% from the Public Works Loans Board for the plan period 2011/15, based on a mix of borrowing terms; and sets a range of prudential indicators which the Director of Finance monitors. This target rate is still achievable should the council decide to borrow.

3. **OPTIONS FOR CONSIDERATION**

- 3.1 The report considers the implementation of an agreed strategy. There are therefore no options to consider.

4. **ANALYSIS OF OPTIONS**

Investment strategy

- 4.1 Markets have been volatile with recurring concerns about economic recovery principally in Europe, the ability of sovereign governments to sustain the burden of debt, and the implications for the solvency of the banking sector. Therefore the focus of cash management has been to maximise security and liquidity. Cash is currently being held primarily in a range of call accounts with UK banks or occasionally as short-term investments with other local authorities and the Debt Management Office.
- 4.2 All investments due to be realised during the period were returned with interest or reinvested. At the end of February outstanding investments were £17.1m including £1.7m with the council's own bankers (**see appendix 1 and 1A**).
- 4.3 The historically low base rate means returns on investments continue to be very modest, an average of 0.60% achieved to date in 2011/12 against a base rate in the same period of 0.5% and a budget target of 1%. There is therefore a forecast shortfall in investment returns of around £144k against the original budget. The shortfall is more than covered by a reduction in borrowing costs.

Borrowing strategy

- 4.4 In line with the approved strategy, there has been no new borrowing to finance the capital programme. Long-term borrowing rates (25 year fixed) have not reached the 6% trigger point set in the strategy, indeed rates are currently falling, and the differential between borrowing and lending rates has not narrowed to 2%. This is the fourth year in which

the council has used cash balances to fund capital investment, and the saving on debt costs has been factored into the budget.

- 4.5 Scheduled debt repayments continue and further to payments due before the year end, the debt outstanding by 31st March, 2012 will be £110.8m.
- 4.6 The added benefit of this approach is to progressively reduce the amount of cash exposed to risk in the financial markets and the underlying balance is reducing (£17.9m in February, gross of Icelandic investments, £17.1m after impairment).
- 4.7 Key performance indicators have been updated following the rephrasing of the capital programme approved at Cabinet on 24 January, 2012. These are shown at **appendix 2**.

Icelandic Investments

- 4.8 The council has taken steps to recover investments with Icelandic banks in concert with other local authorities through the Local Government Association.
- 4.9 The council is now likely to recover most of the £5.5m invested in Icelandic banks in 2008. The table below shows the current position for Heritable against a claim of £3.518m. The Heritable Bank administrators paid a tenth dividend in January, and we expect to recover £3m of the original £3.5m investment.

Interim Payment Number	Date Received	Cumulative Pence in the Pound Received p	Cumulative Amount Received £	Cumulative Amount Received £
Total Approved Claim (Principal + Interest)				
1	30.07.09	16.13	567,384	567,384
2	18.12.09	28.79	445,414	1,012,798
3	30.03.10	34.98	217,899	1,230,697
4	16.07.10	41.25	220,761	1,451,458
5	18.10.10	45.39	145,571	1,597,029
6	14.01.11	50.11	165,964	1,762,993
7	19.04.11	56.36	219,956	1,982,949
8	15.07.11	60.42	142,759	2,125,708
9	20.10.11	64.60	147,119	2,272,827
10	23.01.12	67.92	116,955	2,389,782

The next interim dividend is expected in April 2012.

- 4.10 The Icelandic Supreme Court upheld the judgement that local authorities are priority creditors in respect of investments made with

Landsbanki and, over time, a return of over 95 pence in the pound of the £2m invested is likely. As such, the first distribution has now been received in the sum of £591,177, around one third of the ultimate recoverable amount.

5. RESOURCE IMPLICATIONS

5.1 The financing budget is in balance for 2011/12, but will need to be reconsidered for future years if very low interest returns persist as anticipated. A positive outcome is still expected on the return of Icelandic investments. Over two thirds of the investment in Heritable Bank has now been realised with further repayments scheduled; and the first distribution of repayments of the Landsbanki investments has also now been received.

6. OTHER IMPLICATIONS

6.1 The agreed treasury strategy aims to minimise risk to the council finances from any further instability in financial markets.

7. OUTCOMES OF CONSULTATION

7.1 Not applicable.

8. RECOMMENDATIONS

8.1 That the Audit Sub Committee consider the assurance provided by this report on the effectiveness of arrangements for treasury management, and;

8.2 That the Audit Sub Committee notes the treasury management performance for the period.

DIRECTOR OF FINANCE

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Background Papers used in the preparation of this report

LAAP Bulletin 82 'Guidance on the impairment of deposits with Icelandic banks',
CIPFA – Treasury Management in the Public Services. Code of Practice and Cross-Sectoral Guidance Notes: Fully Revised Second Edition 2009.
CIPFA –The Prudential Code for Capital Finance on Local Authorities; Fully Revised Second Edition 2009

INVESTMENT POSITION AS AT 29 FEBRUARY 2012

CALL ACCOUNT BALANCES	£	
Santander UK plc Call Account	8,388	On call
Barclays Bank plc Call Account	5,000,000	On call
Bank of Scotland Plc Call Account	2,978,872	On call
HSBC Bank Plc Call Account	2,906,982	On call
National Westminster Bank Plc Special Interest Bearing Account	1,730,405	On call
 OTHER INVESTMENTS		
Debt Management Office	2,750,000	Repayment at term
Heritable Bank Limited	1,123,326	In administration
Landsbanki Islands	1,417,162	In receivership
SUB-TOTAL	17,915,135	
LESS:		
Impairments brought to account in 2010/11 relating to Icelandic Investments	852,528	
TOTAL	17,062,607	

APPENDIX 1A

INVESTMENTS MADE AND REALISED APRIL 2011 TO 29 FEBRUARY 2012

INVESTMENT INSTITUTION	DATE INVESTED	AMOUNT	STATUS/DUE DATE OF PAYMENT
INVESTMENTS MADE SINCE 1 APRIL 2011			£
Birmingham City Council	28/06/2011	3,000,000	Repaid
Birmingham City Council	06/09/2011	5,000,000	Repaid
Birmingham City Council	11/10/2011	5,000,000	Repaid
Birmingham City Council	11/11/2011	5,000,000	Repaid
Birmingham City Council	12/12/2011	5,000,000	Repaid
City of Plymouth Council	04/04/2011	5,000,000	Repaid
City of Plymouth Council	10/05/2011	3,000,000	Repaid
Conwy County Borough Council	15/04/2011	3,000,000	Repaid
Coventry Building Society	14/04/2011	3,000,000	Repaid
Coventry Building Society	03/05/2011	3,000,000	Repaid
Debt Management Office	26/04/2011	1,000,000	Repaid
Debt Management Office	04/05/2011	2,400,000	Repaid
Debt Management Office	05/05/2011	2,000,000	Repaid
Debt Management Office	05/05/2011	4,635,000	Repaid
Debt Management Office	09/05/2011	1,000,000	Repaid
Debt Management Office	11/05/2011	1,000,000	Repaid
Debt Management Office	18/05/2011	1,000,000	Repaid
Debt Management Office	19/05/2011	2,500,000	Repaid
Debt Management Office	01/06/2011	2,000,000	Repaid
Debt Management Office	07/06/2011	3,000,000	Repaid
Debt Management Office	15/06/2011	1,500,000	Repaid
Debt Management Office	23/06/2011	1,000,000	Repaid
Debt Management Office	07/07/2011	5,160,000	Repaid
Debt Management Office	11/07/2011	1,000,000	Repaid
Debt Management Office	15/07/2011	2,765,000	Repaid
Debt Management Office	19/07/2011	3,500,000	Repaid
Debt Management Office	19/07/2011	3,500,000	Repaid
Debt Management Office	28/07/2011	1,250,000	Repaid
Debt Management Office	01/08/2011	4,850,000	Repaid
Debt Management Office	02/08/2011	3,167,000	Repaid
Debt Management Office	03/08/2011	3,000,000	Repaid
Debt Management Office	15/08/2011	1,000,000	Repaid
Debt Management Office	26/08/2011	1,500,000	Repaid
Debt Management Office	01/09/2011	8,000,000	Repaid
Debt Management Office	07/09/2011	1,000,000	Repaid
Debt Management Office	15/09/2011	4,500,000	Repaid
Debt Management Office	20/09/2011	1,590,000	Repaid
Debt Management Office	22/09/2011	5,500,000	Repaid
Debt Management Office	07/10/2011	5,000,000	Repaid
Debt Management Office	07/10/2011	5,000,000	Repaid
Debt Management Office	17/10/2011	3,000,000	Repaid
Debt Management Office	17/10/2011	1,000,000	Repaid
Debt Management Office	02/11/2011	3,000,000	Repaid
Debt Management Office	03/11/2011	2,000,000	Repaid
Debt Management Office	02/11/2011	3,000,000	Repaid
Debt Management Office	03/11/2011	2,000,000	Repaid
Debt Management Office	07/11/2011	3,000,000	Repaid
Debt Management Office	14/11/2011	5,000,000	Repaid
Debt Management Office	14/11/2011	5,000,000	Repaid
Debt Management Office	15/11/2011	3,490,000	Repaid
Debt Management Office	18/11/2011	2,500,000	Repaid
Debt Management Office	21/11/2011	2,000,000	Repaid
Debt Management Office	01/12/2011	5,000,000	Repaid
Debt Management Office	01/12/2011	1,000,000	Repaid
Debt Management Office	01/12/2011	1,500,000	Repaid
Debt Management Office	08/12/2011	2,000,000	Repaid
Debt Management Office	14/12/2011	5,000,000	Repaid
Debt Management Office	15/12/2011	5,000,000	Repaid
Debt Management Office	16/12/2011	4,500,000	Repaid
Debt Management Office	19/12/2011	3,500,000	Repaid
Debt Management Office	19/12/2011	1,000,000	Repaid
Debt Management Office	28/12/2011	1,500,000	Repaid

INVESTMENT INSTITUTION	DATE INVESTED	AMOUNT	STATUS/DUE DATE OF PAYMENT
Debt Management Office	30/12/2011	1,000,000	Repaid
Debt Management Office	03/01/2012	4,700,000	Repaid
Debt Management Office	04/01/2012	1,000,000	Repaid
Debt Management Office	05/01/2012	2,000,000	Repaid
Debt Management Office	05/01/2012	1,000,000	Repaid
Debt Management Office	13/01/2012	4,000,000	Repaid
Debt Management Office	16/01/2012	3,250,000	Repaid
Debt Management Office	17/01/2012	2,500,000	Repaid
Debt Management Office	18/01/2012	3,500,000	Repaid
Debt Management Office	23/01/2012	2,000,000	Repaid
Debt Management Office	27/01/2012	1,500,000	Repaid
Debt Management Office	02/02/2012	1,000,000	Repaid
Debt Management Office	02/02/2012	2,000,000	Repaid
Debt Management Office	02/02/2012	2,500,000	02/03/2012
Debt Management Office	08/02/2012	250,000	06/03/2012
Debt Management Office	14/02/2012	1,550,000	Repaid
Debt Management Office	15/02/2012	4,697,000	Repaid
Debt Management Office	17/02/2012	1,000,000	Repaid
Dumfries & Galloway Council	03/05/2011	3,000,000	Repaid
Hertfordshire County Council	17/06/2011	3,000,000	Repaid
Lancashire County Council	15/04/2011	2,000,000	Repaid
Nationwide Building Society	04/04/2011	3,000,000	Repaid
Nationwide Building Society	14/04/2011	2,000,000	Repaid
Nationwide Building Society	28/04/2011	3,000,000	Repaid
Nationwide Building Society	20/05/2011	2,000,000	Repaid
Nationwide Building Society	27/05/2011	3,000,000	Repaid
Nationwide Building Society	01/07/2011	2,000,000	Repaid
Nationwide Building Society	04/07/2011	3,000,000	Repaid
Newcastle City Council	31/05/2011	5,000,000	Repaid
Newcastle City Council	07/06/2011	5,000,000	Repaid
Northamptonshire County Council	20/12/2011	5,000,000	Repaid
Plymouth City Council	07/06/2011	3,000,000	Repaid
Plymouth City Council	27/06/2011	2,000,000	Repaid
Plymouth City Council	07/07/2011	3,000,000	Repaid
Plymouth City Council	27/07/2011	2,000,000	Repaid
Plymouth City Council	08/08/2011	3,000,000	Repaid
Salford City Council	13/05/2011	2,000,000	Repaid
Salford City Council	27/05/2011	2,000,000	Repaid
Salford City Council	14/10/2011	5,000,000	Repaid
Southampton City Council	22/07/2011	2,300,000	Repaid
Stockport Metropolitan Borough Council	26/05/2011	2,000,000	Repaid
Thurrock Borough Council	03/08/2011	4,500,000	Repaid
Torfaen County Borough Council	22/07/2011	3,000,000	Repaid
West Yorkshire Police Authority	18/11/2011	5,000,000	Repaid
INVESTMENTS MADE BEFORE 1 APRIL 2011			
Heritable bank Limited	01/09/2008	989,921	In administration
Heritable bank Limited	12/09/2008	395,968	In administration
Landsbanki Islands	08/08/2008	1,000,000	In receivership
Landsbanki Islands	01/09/2008	1,000,000	In receivership
Salford City Council	15/03/2011	3,500,000	Repaid

APPROVED PRUDENTIAL GUIDELINE INDICATORS

APPENDIX 2

	2011/12 Budget	2011/12 Revised
(i) estimates of capital expenditure	£'000 68,738	£'000 63,440
(ii) General Fund ratio of financing costs to the net revenue stream %	5.4	4.9
(iii) an estimate of the capital financing requirement	£m 159,000	£m no change
(iv) the authorised limit for external debt borrowing other long term liabilities total	253,000 5,000 258,000	no change
(v) the operational boundary for external debt borrowing other long term liabilities total	172,000 5,000 177,000	no change
(vi) upper limit for fixed rate exposure	% 100	no change
(vii) upper limit for variable rate exposure	20	no change
(viii) upper and lower limits for maturity structure of borrowing UPPER LIMIT under 12 months 12 months and within 24 months 24 months and within 5 years 5 years and within 10 years 10 years and above LOWER LIMIT under 12 months 12 months and within 24 months 24 months and within 5 years 5 years and within 10 years 10 years and above	15 15 50 75 90 0 0 0 0 25	no change no change
(ix) total principal sums invested for periods longer than 364 days	£000 0	£000 0

No changes have been made to the parameters for borrowing in 2011/12. These limits were set in the treasury strategy and give authority to borrow should this be required

The change in capital spending is largely a timing issue with rephasing between 2010/11 and 2011/12