

NORTH LINCOLNSHIRE COUNCIL

AUDIT COMMITTEE

QUARTERLY TREASURY MANAGEMENT AND STRATEGY REPORT

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 and August 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

- 1.2 2.1 The **investment strategy for 2012/2013** aims to reduce risk by
 - Investing for shorter periods up to six months
 - Only investing in UK institutions with a minimum of an adequate credit rating or equivalent
 - Applying a maximum investment limit of £5m for most counterparties
 - Applying a maximum limit to financial groups rather than separate institutions
 - Removing any foreign institutions from the counterparty list.
- 2.2 The **borrowing strategy for 2012/2013** aims to
 - Suspend external 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 remain at this all-time low until 2013.
- 2.4 The budget also projects an average cost of external borrowing of 5% from the Public Works Loans Board in later years when internal borrowing is no longer an option, based on a mix of borrowing terms; and sets a range of prudential indicators which the Director of Policy & Resources 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 the reversal of any economic recovery resulting in both the U.K. and Europe slipping into a double-dip recession, the ability of governments to sustain the burden of debt culminating in the possibility of one or more euro-zone periphery countries being forced to leave the single currency with the likely turmoil and uncertainty this would cause, 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 in a range of call accounts with UK banks, on short (1 month maximum) deposit with building societies who maintain an adequate credit rating or as short-term (6 month maximum) 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 August outstanding investments were £30.6m, including £7.9m 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 0.5% achieved in 2012/13 year to date against a base rate in the same period of 0.5% and a budget target of a similar level. The current forecast is that this level of income will be achieved over the year.

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% upper trigger point, but rates have fallen below the 4 % lower trigger points set in the strategy. The differential between borrowing and lending rates has not narrowed to 2%. A judgement has been made that internal borrowing continues to give best value for money. This is the fifth 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 by the end of September further repayments of £1.3m will reduce debt outstanding to £109.5m, with this reducing yet further to £108.9m by March 2013.
- 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 (£30.6m in August, gross of Icelandic investments, £29.3m after impairment).
- 4.7 Key performance indicators have been updated following the rephrasing of the capital programme approved at Cabinet on 25 September 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 acting through the Local Government Association. The administration of Heritable is progressing well. The latest advice is to expect a return of between 85 and 90 pence in the pound. The position with Landsbanki had been in doubt as other creditors had made a legal challenge to the preferential creditor status UK and Dutch Local Authorities had been granted by the Landsbanki Winding Up Board. The Icelandic Supreme Court upheld the preferential status of the Local Authorities and full recovery is now anticipated. Total recovery over all Icelandic investments is currently estimated to be £5.03m at a rate of 90.6%.

Institution	Claim	Paid	Estimated Recovery
Heritable	£3.52m	£2.62m	£3.00m
Landsbanki	£2.03m	£0.86m	£2.03m
	£5.55m	£3.48m	£5.03m

Dividends continue to be received from both Heritable and Landsbanki.

5. RESOURCE IMPLICATIONS

- 5.1 The projected revenue costs of financing debt is within budget. A positive outcome is still expected on the return of Icelandic investments as around three quarters of the investment in Heritable Bank has now been realised, and well over a third of the Landsbanki investment now recovered.
- 5.2 There has been an increase of £4m in the capital programme for 2012/13 (see Appendix 2) largely due to a rephasing of schemes spending from 2011/12, and some changes to programme financing. This is reflected in Appendix 2.

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 Committee consider the assurance provided by this report on the effectiveness of arrangements for treasury management, and;
- 8.2 That the Audit Committee notes the treasury management performance for the period.

DIRECTOR OF POLICY & RESOURCES

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Date: 5 September 2012

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 31 AUGUST 2012

CALL ACCOUNT BALANCES	£	
Barclays Bank plc Call Account	5,000,000	On call
Bank of Scotland Plc Call Account	4,959,416	On call
HSBC Bank Plc Call Account	4,912,103	On call
National Westminster Bank Plc Special Interest Bearing Account	7,919,486	On call
 OTHER INVESTMENTS		
Northern Rock Plc	3,000,000	Repayment at term
Nationwide Building Society	1,500,000	Repayment at term
Coventry Building Society	2,000,000	Repayment at term
Heritable Bank Limited	891,029	In administration
Landsbanki Islands	1,172,477	In receivership
SUB-TOTAL	31,354,512	
LESS:		
Impairments brought to account in 2011/12 relating to Icelandic Investments	752,422	
TOTAL	30,602,090	

APPENDIX 1A

INVESTMENTS MADE AND REALISED APRIL 2012 TO 31 AUGUST 2012

INVESTMENT INSTITUTION	DATE INVESTED	AMOUNT	STATUS/DUE DATE OF PAYMENT
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INVESTMENTS MADE SINCE 1 APRIL 2012

£

Co-Operative Bank Plc	12/04/2012	2,000,000.00	Repaid
Coventry Building Society	04/04/2012	3,000,000.00	Repaid
Coventry Building Society	12/04/2012	2,000,000.00	Repaid
Coventry Building Society	03/05/2012	2,000,000.00	Repaid
Coventry Building Society	08/05/2012	2,000,000.00	Repaid
Coventry Building Society	15/05/2012	1,000,000.00	Repaid
Coventry Building Society	18/05/2012	2,000,000.00	Repaid
Coventry Building Society	21/05/2012	2,000,000.00	Repaid
Coventry Building Society	25/05/2012	2,000,000.00	Repaid
Coventry Building Society	01/06/2012	2,000,000.00	Repaid
Coventry Building Society	01/06/2012	2,000,000.00	Repaid
Coventry Building Society	08/06/2012	2,000,000.00	Repaid
Coventry Building Society	08/06/2012	2,000,000.00	Repaid
Coventry Building Society	15/06/2012	2,000,000.00	Repaid
Coventry Building Society	15/06/2012	1,000,000.00	Repaid
Coventry Building Society	15/06/2012	2,000,000.00	Repaid
Coventry Building Society	22/06/2012	1,000,000.00	Repaid
Coventry Building Society	22/06/2012	2,000,000.00	Repaid
Coventry Building Society	22/06/2012	2,000,000.00	Repaid
Coventry Building Society	29/06/2012	2,000,000.00	Repaid
Coventry Building Society	02/07/2012	2,000,000.00	Repaid
Coventry Building Society	02/07/2012	1,000,000.00	Repaid
Coventry Building Society	06/07/2012	2,000,000.00	Repaid
Coventry Building Society	09/07/2012	2,000,000.00	Repaid
Coventry Building Society	09/07/2012	1,000,000.00	Repaid
Coventry Building Society	13/07/2012	2,000,000.00	Repaid
Coventry Building Society	16/07/2012	2,000,000.00	Repaid
Coventry Building Society	16/07/2012	1,000,000.00	Repaid
Coventry Building Society	23/07/2012	2,000,000.00	Repaid
Coventry Building Society	23/07/2012	1,000,000.00	Repaid
Coventry Building Society	26/07/2012	2,500,000.00	Repaid
Coventry Building Society	30/07/2012	2,000,000.00	Repaid
Coventry Building Society	02/08/2012	3,000,000.00	Repaid
Coventry Building Society	06/08/2012	2,000,000.00	Repaid
Coventry Building Society	09/08/2012	3,000,000.00	Repaid
Coventry Building Society	13/08/2012	2,000,000.00	Repaid
Coventry Building Society	16/08/2012	3,000,000.00	Repaid
Coventry Building Society	20/08/2012	2,000,000.00	Repaid
Coventry Building Society	28/08/2012	2,000,000.00	04/09/2012
Debt Management Office	16/04/2012	1,000,000.00	Repaid
Debt Management Office	16/05/2012	1,000,000.00	Repaid
Debt Management Office	17/05/2012	1,000,000.00	Repaid
Debt Management Office	25/05/2012	2,500,000.00	Repaid
Debt Management Office	01/06/2012	2,000,000.00	Repaid
Debt Management Office	01/06/2012	480,000.00	Repaid
Debt Management Office	06/06/2012	3,428,000.00	Repaid
Debt Management Office	07/06/2012	4,000,000.00	Repaid
Debt Management Office	15/06/2012	1,500,000.00	Repaid

INVESTMENT INSTITUTION	DATE INVESTED	AMOUNT	STATUS/DUE DATE OF PAYMENT
Debt Management Office	19/06/2012	1,500,000.00	Repaid
Debt Management Office	25/06/2012	2,108,000.00	Repaid
Debt Management Office	02/07/2012	1,500,000.00	Repaid
Debt Management Office	04/07/2012	4,000,000.00	Repaid
Debt Management Office	05/07/2012	1,500,000.00	Repaid
Debt Management Office	09/07/2012	1,460,000.00	Repaid
Debt Management Office	16/07/2012	4,000,000.00	Repaid
Debt Management Office	27/07/2012	1,000,000.00	Repaid
Debt Management Office	01/08/2012	2,500,000.00	Repaid
Debt Management Office	01/08/2012	2,000,000.00	Repaid
Debt Management Office	03/08/2012	2,500,000.00	Repaid
Debt Management Office	07/08/2012	1,000,000.00	Repaid
Debt Management Office	08/08/2012	500,000.00	Repaid
Debt Management Office	15/08/2012	3,000,000.00	Repaid
Debt Management Office	22/08/2012	3,000,000.00	Repaid
Nationwide Building Society	04/04/2012	5,000,000.00	Repaid
Nationwide Building Society	04/05/2012	5,000,000.00	Repaid
Nationwide Building Society	15/08/2012	1,500,000.00	17/09/2012
Northern Rock Plc	26/04/2012	1,000,000.00	Repaid
Northern Rock Plc	01/05/2012	2,000,000.00	Repaid
Northern Rock Plc	30/05/2012	1,000,000.00	Repaid
Northern Rock Plc	01/06/2012	2,000,000.00	Repaid
Northern Rock Plc	06/06/2012	1,000,000.00	Repaid
Northern Rock Plc	08/06/2012	2,000,000.00	Repaid
Northern Rock Plc	13/06/2012	1,000,000.00	Repaid
Northern Rock Plc	15/06/2012	2,000,000.00	Repaid
Northern Rock Plc	20/06/2012	1,000,000.00	Repaid
Northern Rock Plc	22/06/2012	2,000,000.00	Repaid
Northern Rock Plc	27/06/2012	1,000,000.00	Repaid
Northern Rock Plc	29/06/2012	2,000,000.00	Repaid
Northern Rock Plc	04/07/2012	1,000,000.00	Repaid
Northern Rock Plc	06/07/2012	2,000,000.00	Repaid
Northern Rock Plc	11/07/2012	1,000,000.00	Repaid
Northern Rock Plc	13/07/2012	2,000,000.00	Repaid
Northern Rock Plc	23/07/2012	3,000,000.00	Repaid
Northern Rock Plc	30/07/2012	3,000,000.00	Repaid
Northern Rock Plc	06/08/2012	3,000,000.00	Repaid
Northern Rock Plc	13/08/2012	2,000,000.00	Repaid
Northern Rock Plc	17/08/2012	1,000,000.00	Repaid
Northern Rock Plc	20/08/2012	2,000,000.00	Repaid
Northern Rock Plc	24/08/2012	1,000,000.00	Repaid
Northern Rock Plc	28/08/2012	2,000,000.00	04/09/2012
Northern Rock Plc	24/08/2012	1,000,000.00	07/09/2012

INVESTMENTS MADE BEFORE 1 APRIL 2012

Heritable bank Limited	01/09/2008	802,376	In administration
Heritable bank Limited	12/09/2008	320,950	In administration
Landsbanki Islands	08/08/2008	708,581	In receivership
Landsbanki Islands	01/09/2008	708,581	In receivership

APPROVED PRUDENTIAL GUIDELINE INDICATORS

APPENDIX 2

	2012/13 Budget	2012/13 Revised
(i) estimates of capital expenditure	£'000 47,166	£'000 50,905
(ii) General Fund ratio of financing costs to the net revenue stream % (Based on Prudential Code 2011)	7.77	7.83
(iii) an estimate of the capital financing requirement	£m 164,744	£m 165,741
(iv) the authorised limit for external debt borrowing other long term liabilities total	228,000 5,000 233,000	no change
(v) the operational boundary for external debt borrowing other long term liabilities total	171,000 2,000 173,000	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

The change in capital spending is largely a timing issue with a rephasing between 2011/12 and later financial years.