

NORTH LINCOLNSHIRE COUNCIL

AUDIT SUB-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 December 2011. 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.

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 in a range of call accounts with UK banks or as short-term investments with other local authorities and the Debt Management Office.

4.2 Following downgradings of the credit ratings produced by the three major credit ratings agencies, the amounts held with any of the institutions affected, including our own bankers has been reduced in line with the current Treasury Management strategy policy.

4.2 All investments due to be realised during the period were returned with interest or reinvested. At the end of December outstanding investments were £26.1m (£23.8m excluding Icelandic investments), including £4.4m 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 £130k this year with a further adjustment needed to our future forecasts. The shortfall is covered in 2011/12 by a reduction in the minimum revenue provision.

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 the current debt outstanding is now £111.4m.
- 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 (£27.0m in December, gross of Icelandic investments, £26.1m after impairment).
- 4.7 Key performance indicators have been updated following the rephasing of the capital programme approved at Cabinet on 27 September 2011. 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 ninth dividend in October, 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

The next interim dividend is expected in January 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. The first distribution is imminent.

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. Almost 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 being anticipated shortly.

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 31 DECEMBER 2011

CALL ACCOUNT BALANCES	£	
Santander UK plc Call Account	8,388	On call
Barclays Bank plc Call Account	3,000,000	On call
Bank of Scotland Plc Call Account	977,206	On call
HSBC Bank Plc Call Account	1,905,748	On call
National Westminster Bank Plc Special Interest Bearing Account	4,366,975	On call
 OTHER INVESTMENTS		
Debt Management Office	3,500,000	Repayment at term
Birmingham City Council	5,000,000	Repayment at term
Northamptonshire County Council	5,000,000	Repayment at term
Heritable bank Limited	1,239,612	In administration
Landsbanki Islands	2,000,000	In receivership
SUB-TOTAL	26,997,929	
LESS:		
Impairments brought to account in 2010/11 relating to Icelandic Investments	852,528	
TOTAL	26,145,400	

APPENDIX 1A

INVESTMENTS MADE AND REALISED APRIL 2011 TO 31 DECEMBER 2011

INVESTMENT INSTITUTION	DATE INVESTED	AMOUNT	STATUS/DUE DATE OF PAYMENT
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INVESTMENTS MADE SINCE 1 APRIL 2011

£

Birmingham City Council	28/06/2011	3,000,000.00	Repaid
Birmingham City Council	06/09/2011	5,000,000.00	Repaid
Birmingham City Council	11/10/2011	5,000,000.00	Repaid
Birmingham City Council	11/11/2011	5,000,000.00	Repaid
Birmingham City Council	12/12/2011	5,000,000.00	13/01/2012
City of Plymouth Council	04/04/2011	5,000,000.00	Repaid
City of Plymouth Council	10/05/2011	3,000,000.00	Repaid
Conwy County Borough Council	15/04/2011	3,000,000.00	Repaid
Coventry Building Society	14/04/2011	3,000,000.00	Repaid
Coventry Building Society	03/05/2011	3,000,000.00	Repaid
Debt Management Office	26/04/2011	1,000,000.00	Repaid
Debt Management Office	04/05/2011	2,400,000.00	Repaid
Debt Management Office	05/05/2011	2,000,000.00	Repaid
Debt Management Office	05/05/2011	4,635,000.00	Repaid
Debt Management Office	09/05/2011	1,000,000.00	Repaid
Debt Management Office	11/05/2011	1,000,000.00	Repaid
Debt Management Office	18/05/2011	1,000,000.00	Repaid
Debt Management Office	19/05/2011	2,500,000.00	Repaid
Debt Management Office	01/06/2011	2,000,000.00	Repaid
Debt Management Office	07/06/2011	3,000,000.00	Repaid
Debt Management Office	15/06/2011	1,500,000.00	Repaid
Debt Management Office	23/06/2011	1,000,000.00	Repaid
Debt Management Office	07/07/2011	5,160,000.00	Repaid
Debt Management Office	11/07/2011	1,000,000.00	Repaid
Debt Management Office	15/07/2011	2,765,000.00	Repaid
Debt Management Office	19/07/2011	3,500,000.00	Repaid
Debt Management Office	19/07/2011	3,500,000.00	Repaid
Debt Management Office	28/07/2011	1,250,000.00	Repaid
Debt Management Office	01/08/2011	4,850,000.00	Repaid
Debt Management Office	02/08/2011	3,167,000.00	Repaid
Debt Management Office	03/08/2011	3,000,000.00	Repaid
Debt Management Office	15/08/2011	1,000,000.00	Repaid
Debt Management Office	26/08/2011	1,500,000.00	Repaid
Debt Management Office	01/09/2011	8,000,000.00	Repaid
Debt Management Office	07/09/2011	1,000,000.00	Repaid
Debt Management Office	15/09/2011	4,500,000.00	Repaid
Debt Management Office	20/09/2011	1,590,000.00	Repaid
Debt Management Office	22/09/2011	5,500,000.00	Repaid
Debt Management Office	07/10/2011	5,000,000.00	Repaid
Debt Management Office	07/10/2011	5,000,000.00	Repaid
Debt Management Office	17/10/2011	3,000,000.00	Repaid
Debt Management Office	17/10/2011	1,000,000.00	Repaid
Debt Management Office	02/11/2011	3,000,000.00	Repaid
Debt Management Office	03/11/2011	2,000,000.00	Repaid
Debt Management Office	02/11/2011	3,000,000.00	Repaid
Debt Management Office	03/11/2011	2,000,000.00	Repaid
Debt Management Office	07/11/2011	3,000,000.00	Repaid
Debt Management Office	14/11/2011	5,000,000.00	Repaid
Debt Management Office	14/11/2011	5,000,000.00	Repaid

Debt Management Office	15/11/2011	3,490,000.00	Repaid
Debt Management Office	18/11/2011	2,500,000.00	Repaid
Debt Management Office	21/11/2011	2,000,000.00	Repaid
Debt Management Office	01/12/2011	5,000,000.00	23.12.11
Debt Management Office	01/12/2011	1,000,000.00	Repaid
Debt Management Office	01/12/2011	1,500,000.00	Repaid
Debt Management Office	08/12/2011	2,000,000.00	30/12/2011
Debt Management Office	14/12/2011	5,000,000.00	Repaid
Debt Management Office	15/12/2011	5,000,000.00	30/12/2011
Debt Management Office	16/12/2011	4,500,000.00	Repaid
Debt Management Office	19/12/2011	3,500,000.00	Repaid
Debt Management Office	19/12/2011	1,000,000.00	20/01/2012
Debt Management Office	28/12/2011	1,500,000.00	27/01/2012
Debt Management Office	30/12/2011	1,000,000.00	31/01/2012

Dumfries & Galloway Council 03/05/2011 3,000,000.00 Repaid

Hertfordshire County Council 17/06/2011 3,000,000.00 Repaid

Lancashire County Council 15/04/2011 2,000,000.00 Repaid

Nationwide Building Society 04/04/2011 3,000,000.00 Repaid

Nationwide Building Society 14/04/2011 2,000,000.00 Repaid

Nationwide Building Society 28/04/2011 3,000,000.00 Repaid

Nationwide Building Society 20/05/2011 2,000,000.00 Repaid

Nationwide Building Society 27/05/2011 3,000,000.00 Repaid

Nationwide Building Society 01/07/2011 2,000,000.00 Repaid

Nationwide Building Society 04/07/2011 3,000,000.00 Repaid

Newcastle City Council 31/05/2011 5,000,000.00 Repaid

Newcastle City Council 07/06/2011 5,000,000.00 Repaid

Northamptonshire County Council 20/12/2011 5,000,000.00 17/01/2012

Plymouth City Council 07/06/2011 3,000,000.00 Repaid

Plymouth City Council 27/06/2011 2,000,000.00 Repaid

Plymouth City Council 07/07/2011 3,000,000.00 Repaid

Plymouth City Council 27/07/2011 2,000,000.00 Repaid

Plymouth City Council 08/08/2011 3,000,000.00 Repaid

Salford City Council 13/05/2011 2,000,000.00 Repaid

Salford City Council 27/05/2011 2,000,000.00 Repaid

Salford City Council 14/10/2011 5,000,000.00 Repaid

Southampton City Council 22/07/2011 2,300,000.00 Repaid

Stockport Metropolitan Borough Council 26/05/2011 2,000,000.00 Repaid

Thurrock Borough Council 03/08/2011 4,500,000.00 Repaid

Torfaen County Borough Council 22/07/2011 3,000,000.00 Repaid

West Yorkshire Police Authority 18/11/2011 5,000,000.00 Repaid

INVESTMENTS MADE BEFORE 1 APRIL 2011

Heritable bank Limited 01/09/2008 989,920.87 In administration

Heritable bank Limited 12/09/2008 395,968.34 In administration

Landsbanki Islands 08/08/2008 1,000,000.00 In receivership

Landsbanki Islands 01/09/2008 1,000,000.00 In receivership

Salford City Council 15/03/2011 3,500,000.00 Repaid

