Audit Committee		Agenda Item:
Meeting Date	19 December 2012	
Report Title	Treasury Management Half Year Report	
Portfolio Holder	Cabinet Member for Finance: Cllr Duncan Dewar-Whalley	
SMT Lead	Nick Vickers, Head of Finance	
Head of Service	Nick Vickers, Head of Finance	
Lead Officer	Deborah Walton, Senior Accountant	
Key Decision	No	
Classification	Reference number:	
Recommendations	1. To note the performance information in this report.	

1 Purpose of Report and Executive Summary

1.1 The purpose of this report is to review the mid year outturn position on treasury management transactions for 2012/13 including compliance with treasury limits and Prudential Performance Indicators. The report was submitted to Cabinet on 5 December and will go to Council on 9 January.

1.2 The Treasury Management Strategy is underpinned by the adoption of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management. In accordance with the Code of Practice members are informed of Treasury Management activities twice a year.

1.3 The approach to the use of the cash surplus continues to be highly risk averse both in terms of the counterparties the Council will use and the duration of deposits.

2 Background

Investment Activity

2.1 The counterparties agreed by Cabinet and Council earlier this year when the 2012/13 Treasury Strategy was agreed are:

- Debt Management Office - Debt Management Account Deposit Facility;
- Gilts (bonds issued by the UK Government);
- AAA rated Money Market Funds; and
- Major UK Financial institutions with a lowest minimum long term credit rating of A- and short term rating of F1, or equivalent:

- Royal Bank of Scotland Plc (RBS);
- National Westminster Bank;
- Lloyds TSB Bank Plc;
- Bank of Scotland Plc;
- Barclays Bank Plc;
- HSBC Bank Plc;
- Santander UK Plc;
- Standard Chartered Bank; and
- Nationwide Building Society.

2.2 The investment activity during the first six months conformed to the approved strategies at all times with no breaches.

2.3 Investments held at 2 November 2012 can be found in Appendix I.

2.4 In June the rating agency Moody's completed its major review of banks with global capital market operations and reduced their long term credit ratings, these included Barclays, HSBC, and RBS. Separately they also downgraded Lloyds, Bank of Scotland, National Westminster and Santander UK. Nonetheless all these banks still met our long term credit rating requirement. Moody's downgrade of the short term rating of RBS and National Westminster led to their suspension from the counterparty list.

2.5 Generally since June there has been an improvement in liquidity in the banking sector based upon action by the Central banks, both the Bank of England and the European Central Bank. The volatility and risk indices which we monitor based on information from Arlingclose are much improved.

2.6 In light of this the Council recommenced use of Santander UK in August and Cabinet agreed to recommence the use of RBS and National Westminster at its meeting in September, both on the recommendation of the Chief Financial Officer.

2.7 Generally we are keeping the duration of deposits short as there is little gain in return from depositing for a longer duration. The Council has made three, 3 month deposits with Lloyds, Barclays and Nationwide which achieve rates of 1.35%, 0.67% and 0.58% respectively.

2.8 The Council did not need to borrow to cover cash flow purposes in the period.

2.9 Interest income received for the first half of 2012 was £16,000 above the original budget of £33,000.

2.10 For the six months to 30 September 2012, the Council maintained an average sum invested of £20.7m compared with an original budget of £10.3m, and an average rate of return of 0.47% compared to a budget of 0.62%.

2.11 The results for the six months to 30 September 2012 show that the Council achieved 0.07% average return below the average 7 day London Interbank Bid Rate (LIBID) and 0.03% average return rate below the Bank of England Base Rate.

2.12 We will review counterparty limits for 2013/14, as with our higher cash balances we are using counterparties paying very low rates.

Compliance with Prudential Indicators

2.13 The Council can confirm that it has complied with its Prudential Indicators for 2012/13 which were set in February as part of the Council's Treasury Management Strategy Statement.

2.14 Prudential Indicators are set out in Appendix II.

3. Alternative Options

3.1 The Head of Finance will consider changes to the counterparty criteria with reference to the Council's agreed policy with regard to risk.

4. Consultation Undertaken

4.1 Consultation has been undertaken with the Council's treasury management advisor Arlingclose.

5. Implications

Issue	**Implications**
Corporate Plan	No direct application.
Financial, Resource and Property	As detailed in the report.
Legal and Statutory	The Council has powers to both borrow funds to support its work and to invest and earn interest on funds available.
Crime and Disorder	Following CIPFA's Treasury Management Code of Practice is important to avoid involvement in potential fraud or money laundering.
Risk Management and Health and Safety	Risk is controlled through adherence to specific guidance included in CIPFA's Treasury Management Code of Practice. The principle of security of funds over-rides investment performance.
Equality and Diversity	None
Sustainability	None

6. Appendices

6.1 The following documents are to be published with this report and form part of the report.

- Appendix I: Investments as at 2 November 2012
- Appendix II: Prudential Indicators

7. Background Papers

7.1 The background papers are held by Finance and include:

- Prudential Code for Capital Finance in Local Authorities (2011 Edition) – CIPFA
- Treasury Management in the Public Services Code of Practice and Cross Sectional Guidance Notes (2011 Edition) – CIPFA
- Treasury Management in the Public Services Guidance Notes for Local Authorities including Police Authorities and Fire Authorities (2011 Edition) – CIPFA
- Treasury Management Strategy Statement and Investment Strategy 2012/13
- Arlingclose – Economic and Interest Rate Outlook

Investments as at 2 November 2012

Counterparty/ Country	Short Term Rating (Fitch)	Long Term Rating (Fitch)	Balance Invested as at 2 November 2012 £000s
			Up to 1 month
Banks - UK			
Barclays Bank Plc	F1	A	2,000
HSBC Bank Plc	F1+	AA	2,000
Lloyds Bank TSB	F1	A	2,000
Royal Bank of Scotland (Call Account)	F1	A	2,000
Santander UK (Call Account)	F1	A	2,000
Total Banks			**10,000**
Building Societies - UK			
Nationwide	F1	A+	2,000
Total Building Societies			**2,000**
Debt Management Office			
Debt Management Deposit Account Facility	AAA		1,170
Total Debt Management Office			**1,170**
Money Market Funds (MMFs) - UK			
Goldman Sachs	AAA		2,000
Royal Bank of Scotland	AAA		2,000
Scottish Widows	AAA		1,379
Total MMFs			**5,379**
Total			**18,549**

The Ratings above are from Fitch Ratings. The Long Term Rating is the benchmark measure of probability of default. The Short Term Rating has a time horizon of less than 12 months for most obligations, and thus places greater emphasis on the liquidity necessary to meet financial commitments in a timely manner. These ratings are shown for illustrative purposes only, as the Council uses the lowest rating across three agencies on which to base its decisions.

The deposits for the year to 2 November are summarised below:

Investments	Balance on 01/04/2012 £000s	Investments Made £000s	Investments Repaid £000s	Balance on 02/11/2012 £000s	Average Rate %	Average Life (days)
Short Term Investments	15,423	99,386	(96,260)	18,549	0.49	25
Long Term Investments	3	0	0	3	3.15	Undated
Total Investments	15,426	0	0	18,552		
Increase/(Decrease) in Investments				3,126		

Prudential Indicators

1. Background

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators.

2. Net Debt and the Capital Financing Requirement (CFR)

This is a key indicator of prudence. In order to ensure that over the medium term net debt will only be for a capital purpose, the local authority should ensure that the net debt does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any additional increases to the capital financing requirement for the current and next two financial years.

The Head of Finance reports that the authority had no difficulty meeting this requirement so far in 2012/13, nor is there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3. Estimates of Capital Expenditure

This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax.

Capital Expenditure	**2011/12 Actual £'000**	**2012/13 Original Estimate £'000**	**2013/14 Original Estimate £'000**	**2014/15 Original Estimate £'000**
Total	**1,748**	**1,068**	**941**	**941**

Capital expenditure will be financed follows:

Capital Financing	**2011/12 Actual £'000**	**2012/13 Original Estimate £'000**	**2013/14 Original Estimate £'000**	**2014/15 Original Estimate £'000**
Capital receipts	97	97	0	0
Government Grants	1,540	906	906	906
Revenue contributions	111	65	35	35
Total Financing	**1,748**	**1,068**	**941**	**941**

4. Ratio of Financing Costs to Net Revenue Stream

This is an indicator of affordability, highlighting the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs. The definition of financing costs is set out in the Prudential Code. The ratio is based on costs net of investment income.

Ratio of Financing Costs to Net Revenue Stream	2011/12 Actual %	2012/13 Original Estimate %	2013/14 Original Estimate %	2014/15 Original Estimate %
Total	**4.87**	**5.09**	**4.90**	**4.21**

5. Capital Financing Requirement

The Capital Financing Requirement measures the Council's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and its financing.

Capital Financing Requirement	31/03/12 Actual £'000	31/03/13 Original Estimate £'000	31/03/14 Original Estimate £'000	31/03/15 Original Estimate £'000
Total CFR	**7,170**	**6,326**	**5,502**	**4,776**

6. Actual External Debt

This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities. This Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

Actual External Debt as at 31/03/2012	£'000
Borrowing	0
Other Long-term Liabilities	1,935
Total	**1,935**

7. Incremental Impact of Capital Investment Decisions on Council Tax

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax. The incremental impact is calculated by comparing the total revenue budget requirement of the current approved capital programme with an equivalent calculation of the revenue budget requirement arising from the proposed capital programme.

Incremental Impact of Capital Investment Decisions	2011/12 Actual £	2012/13 Original Estimate £	2013/14 Original Estimate £	2014/15 Original Estimate £
Increase / (Decrease) in Band D Council Tax	(0.14)	(0.01)	(0.02)	(0.00)

8. Authorised Limit and Operational Boundary for External Debt

The Authorised Limit sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities). This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases. It is consistent with the Council's existing commitments, its proposals for capital expenditure and financing, and its approved treasury management policy statement and practices.

The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements.

The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

Authorised Limit for External Debt	2012/13 Original Estimate £'000	2013/14 Original Estimate £'000	2014/15 Original Estimate £'000
Borrowing	5,000	5,000	5,000
Other Long-term Liabilities	2,000	4,000	4,000
Total	**7,000**	**9,000**	**9,000**

The Operational Boundary links directly to the Council's estimates of the CFR and estimates of other cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

Operational Boundary for External Debt	2012/13 Original Estimate £'000	2013/14 Original Estimate £'000	2014/15 Original Estimate £'000
Borrowing	4,000	4,000	4,000
Other Long-term Liabilities	1,719	3,643	3,084
Total	**5,719**	**7,643**	**7,084**

The Head of Finance confirms that there were no breaches to the Authorised Limit and the Operational Boundary during the period to 30 September 2012.

9. Adoption of the CIPFA Treasury Management Code

This indicator demonstrates that the Council has adopted the principles of best practice.

Adoption of the CIPFA Code of Practice in Treasury Management
The Council approved the adoption of the CIPFA Treasury Management Code at its Council meeting on 24 July 2002.

The Council has incorporated the changes from the revised CIPFA Code of Practice into its treasury policies, procedures and practices.

10. Gross and Net Debt

The purpose of this treasury indicator is to highlight a situation where the Council is planning to borrow in advance of need which is not the case for this Council.

Upper Limit on Net Debt compared to Gross Debt	2011/12 Actual £'000	2012/13 Original Estimate £'000	2013/14 Original Estimate £'000	2014/15 Original Estimate £'000
Outstanding Borrowing	0	0	0	0
Other Long-term Liabilities	1,935	1,719	3,643	3,084
Gross Debt	**1,935**	**1,719**	**3,643**	**3,084**
Less: Investments	(15,423)	(6,000)	(6,000)	(6,000)
Net Debt	**(13,488)**	**(4,281)**	**(2,357)**	**(2,916)**

11. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. This Council calculates these limits on net principal outstanding sums, (i.e. fixed rate debt net of fixed rate investments).

Upper Limits for Interest Rate Exposure	**Existing level at 31/03/12** **%**	**2012/13 Approved Limit** **%**	**2013/14 Approved Limit** **%**	**2014/15 Approved Limit** **%**
Interest on fixed rate borrowing	0	100	100	100
Interest on fixed rate investments	-50	-100	-100	-100
Upper Limit for Fixed Interest Rate Exposure	**-50**	**0**	**0**	**0**
Interest on variable rate borrowing	0	100	100	100
Interest on variable rate investments	-50	-100	-100	-100
Upper Limit for Variable Interest Rate Exposure	**-50**	**0**	**0**	**0**

As the Council has no borrowing, these calculations have resulted in a negative figure.

12. Maturity Structure of Fixed Rate borrowing

This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates. It is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

Maturity structure of fixed rate borrowing	**Existing level at 31/03/12** **%**	**Lower Limit for 2012/13** **%**	**Upper Limit for 2012/13** **%**
Under 12 months	0	0	100
12 months and within 24 months	0	0	0
24 months and within 5 years	0	0	0
5 years and within 10 years	0	0	0
10 years and above	0	0	0

The Council does not have any external borrowing for capital purposes, and did not need to borrow for cash flow purposes during the six months to 30 September 2012.

13. Credit Risk

The Council considers security, liquidity and yield, in that order, when making investment decisions.

Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the Council's assessment of counterparty credit risk.

The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- published credit ratings of the financial institution (minimum A- or equivalent) and its sovereign (minimum AA+ or equivalent for non-UK sovereigns);
- sovereign support mechanisms;
- credit default swaps (where quoted);
- share prices (where available);
- economic fundamentals, such as a country's net debt as a percentage of its GDP;
- corporate developments, news, articles, markets sentiment and momentum; and
- subjective overlay.

The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

The Head of Finance confirms that there were no breaches to counterparty limits or credit ratings at the time of placing investments.

14. Upper Limit for total principal sums invested over 364 days

There are currently no proposals for the Council to invest sums for periods longer than 364 days.

15. Investment Benchmarking for the six months to 30 September 2012

Average Actual Return on Investments	Original Estimate Return on Investments	Average Bank Rate	Average 7 day LIBID Rate
0.47%	0.62%	0.50%	0.54%