

 <b>Finance and Audit Scrutiny Committee.</b> <b>16<sup>th</sup> March 2010.</b>		<b>Agenda Item No.</b> <div style="font-size: 2em; float: right;"><b>7</b></div>
<b>Title</b>	Treasury Management Activity Report for the period 1 <sup>st</sup> October 2009 to 31 <sup>st</sup> December 2009.	
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<b>Service Area</b>	Finance	
<b>Wards of the District directly affected</b>	All	
<b>Is the report private and confidential and not for publication by virtue of a paragraph of schedule 12A of the Local Government Act 1972, following the Local Government (Access to Information) (Variation) Order 2006</b>	No	
<b>Date and meeting when issue was last considered and relevant minute number</b>	n/a	
<b>Background Papers</b>	Treasury Management File L2/9 Treasury Management Information via External Advisers, Brokers, External Investment Agents etc.	

<b>Contrary to the policy framework:</b>	No
<b>Contrary to the budgetary framework:</b>	No
<b>Key Decision?</b>	No
<b>Included within the Forward Plan? (If yes include reference number)</b>	No

Officer/Councillor Approval		
With regard to officer approval all reports <i>must</i> be approved by the report authors relevant director, Finance, Legal Services and the relevant Portfolio Holder(s).		
Officer Approval	Date	Name
Relevant Director	26/02/2010	Andy Jones
Chief Executive	N/A	
CMT	N/A	
Section 151 Officer	26/02/2010	Mike Snow
Legal	N/A	
Finance	26/02/2010	Roger Wyton
Portfolio Holder(s)	N/A	
Consultation Undertaken		
Please insert details of any consultation undertaken with regard to this report.		
None		
Final Decision?		Yes
Suggested next steps (if not final decision please set out below)		

## 1. SUMMARY

- 1.1 This report details the Council's Treasury Management Performance for the period 1<sup>st</sup> October 2009 to 31<sup>st</sup> December 2009.

## 2. RECOMMENDATION

- 2.1 That the Members of the Finance and Audit Scrutiny Committee note the contents of this report.

## 3. REASONS FOR THE RECOMMENDATION

- 3.1 The Council's 2009/10 Treasury Management Strategy and Treasury Management Practices (TMP's) require the performance of the Treasury Management Function to be reported to Members on a quarterly basis.
- 3.2 This report informs members of past performance, hence Members are just asked to note the information contained within it.

## 4. ALTERNATIVE OPTION CONSIDERED

- 4.1 None.

## 5. BUDGETARY FRAMEWORK

- 5.1 Treasury Management has a potentially significant impact on the Council's budget through its ability to maximise its investment interest income and minimise borrowing interest payable. The Council is reliant upon interest received to help fund the services it provides and it is anticipated that total interest amounting to £1,072,500 in round terms will be credited to the General Fund in 2009/10. The overall position is shown in the table below:

	<b>Original 2009/10 Budget £</b>	<b>Revised 2009/10 Budget £</b>
Gross Investment Interest	699,200	729,900
Less HRA allocation	(320,900)	(256,700)
	<b>378,300</b>	<b>473,200</b>
Plus VAT interest		599,300
Net interest to General Fund	<b>378,300</b>	<b>1,072,500</b>

## 6. POLICY FRAMEWORK

- 6.1 Treasury Management will support the 2008-11 Corporate Strategy through its contribution to effective management of resources.

## 7. BACKGROUND

- 7.1 The general economic background is important in understanding how markets are behaving. After rapidly cutting interest rates to a historic low of 0.5%, the Monetary Policy Committee (MPC) again increased the amount of asset purchases under the Bank's quantitative easing (QE) programme from £175bn to £200bn in November 2009. While improving liquidity in the financial markets the benefits to the wider economy remain limited.

- 7.2 Activity indicators suggest that the economy is finally exiting the recession, with household spending growing at its fastest rate since early 2008 as consumers brought forward spending before the reinstatement of the standard rate of VAT on 1<sup>st</sup> January 2010. Private car sales were some 141% higher in November than a year ago, partly as a result of the scrappage scheme. Consumer Price Inflation (CPI) rose from 1.1% in September to 1.9% in November, much of this rise being due to energy prices rising. This third quarter also saw improvements in unemployment, the claimant count rose by 5,900 in October but fell by 6,300 in November. This improvement no doubt supported the housing market which continued to recover in quarter three albeit at a slower rate than in quarter two. The third quarter saw the global recovery continue with the strongest recovery being in the US.

## 8. INTEREST RATE ENVIRONMENT

- 8.1. The major influence on the Council's investments is the Bank Rate. The Bank Rate remained at 0.5% for the whole of the quarter ending 31<sup>st</sup> December 2009. The Council's Treasury Management Advisors, Sector, provided the following forecast for future Bank Rates:

	Mar 2010	Jun 2010	Sep 2010	Dec 2010	Mar 2011	June 2011	Sep 2011	Dec 2011	Mar 2012	June 2012	Sept 2012
<b>Current Forecast, as at 22nd February 2010:</b>											
Bank Rate	0.50%	0.50%	0.50%	0.50%	1.00%	1.50%	2.00%	2.50%	3.00%	3.25%	3.75%
<b>Forecast, as at January 2010 when estimates were calculated:</b>											
Bank Rate	0.50%	0.50%	0.75%	1.00%	1.50%	2.25%	2.75%	3.25%	3.50%	3.75%	4.25%
<b>Forecast as at February 2009 when Original Budgets were set:</b>											
Bank Rate	0.75%	1.00%	1.25%	1.75%	2.50%	3.25%	3.75%	4.00%	n/a	n/a	n/a

This current forecast indicates that the Bank Rate will remain at an historical low level for a longer period, with the first increase now not being expected until March 2011, by which time the economy is expected to have improved. This latest forecast shows a slower pace of increase in interest rates over the period than had previously been made, reflecting a less optimistic view on the strength and timing of the economic recovery. The forecast as at January 2010 is shown for comparison purposes as this forecast was used in calculating the estimates. The financial implications of this latest forecast are currently being evaluated.

- 8.2. The Council aims to achieve the optimum return on investments commensurate with the proper levels of security and liquidity. The Annual Investment Strategy 2009/10 was approved by Council on 23<sup>rd</sup> February 2009. This approved the current lending criterion which reflects the level of risk appetite of the Council. However, the Council continues to review its Standard Lending List as a result of frequent changes to Banking Institutions credit ratings, to ensure that it does not lend to those institutions identified as being at risk from the crisis in the banking sector.

## 9 IN HOUSE MANAGED INVESTMENTS

### Money Market Investments

- 9.1. During 2009/10, the in house function has invested in both cash flow driven as well as core cash funds in fixed term deposits in the Money Markets. The table below illustrates the performance of the in house function for each category normally invested in:

Period	Investment Return	LIBID Benchmark	Out/(Under) performance
Up to 7 days			
April to June 2009	No investments made in this quarter.		
July to Sept 2009	No investments made in this quarter.		
Oct to Dec 2009	No investments made in this quarter.		
Over 7 days & Up to 3 Months			
April to June 2009	1.16%	0.89%	+ 0.27%
Value of Interest earned – Q1	£2,706	£2,073	+ £633
July to Sept 2009	1.62%	0.48%	+1.14%
Value of Interest earned – Q2	£16,578	£4,905	+ £11,673
Oct to Dec 2009	0.78%	0.37%	+ 0.41%
Value of Interest earned – Q3	£8,453	£3,952	+ £4,501
3 to 6 Months			
April to June 2009	1.85%	1.30%	+ 0.55%
Value of Interest earned	£11,531	£8,103	+ £3,428
July to Sept 2009	1.18%	0.72%	+0.46%
Value of Interest earned – Q2	£34,493	£21,028	+ £13,465
Oct to Dec 2009	1.19%	0.52%	+ 0.67%
Value of Interest earned – Q3	£56,565	£24,514	+ £32,051
6 Months to 363 days			
April to June 2009	1.35%	1.54%	(0.19%)
Value of Interest earned – Q1	£13,537	£15,422	(£1,885)
July to Sept 2009	1.03%	0.99%	+0.04%
Value of Interest earned – Q2	£5,192	£4,991	+ £201
Oct to Dec 2009	1.00%	0.81%	+ 0.19%
Value of Interest earned – Q3	£7,507	£6,112	+ £1,395
364 days and over			
April to June 2009	2.20%	1.66%	+ 0.54%
Value of Interest earned – Q1	£65,819	£49,664	£16,155
July to Sept 2009	1.46%	1.14%	+0.32%
Value of Interest earned – Q2	£58,438	£45,569	+ £12,869
Oct to Dec 2009	No investments made in this quarter.		

- 9.2. At this time of year, the period for which the Councils cash flow is invested in continues to lengthen as cash is invested to cover immediate cashflow needs, typically around the two to three month period. The Council therefore, made investments in the 1 to 3 month category which did benefit from inflated interest rates and produced an average return of 0.78% compared to the LIBID benchmark of 0.37% which is an amalgam of the 1 and 3 month LIBID rates. This shows an out performance of 0.41%, this was achieved by investing in Building Societies who were paying above the LIBID rates and satisfied the Council's approved investment criteria.
- 9.3. Several core investments matured during the quarter, which were in general invested for three month periods following advice from our Treasury Consultants. Deals placed in the 3 to 6 month category produced an average rate of return of 1.19% which compares to a LIBID benchmark of 0.52% which is an amalgam of the 3 and 6 month LIBID rates. This shows an outperformance of 0.67%.
- 9.4. One six month core investment was placed during the quarter at 1.00% which compares to a LIBID benchmark of 0.81% which is an amalgam of the 6 and 12 month LIBID rates. This shows an out performance of 0.19%. If compared to just the 6 month LIBID benchmark of 0.63% there is an out performance of some 0.37%.
- 9.5. Given that the current Bank Rate is 0.50% the levels of outperformance achieved this quarter are pleasing and reflect the effect that interest rates payable are still above where they should be because of the liquidity concerns in the market.

### **Money Market Funds**

- 9.6. The in house function continues to utilise the Money Market Funds to assist in managing its short term liquidity needs. Their performance in this period is shown in the table below:

<b>Fund</b>	<b>Investment Return</b>	<b>LIBID Benchmark</b>	<b>Out/(Under) Performance</b>
<b>Standard Life</b>			
April to June 2009	0.87%	0.49%	+0.38%
Value of Interest earned – Q1	£3,690	£2,075	+ £1,615
July to Sept 2009	0.50%	0.41%	+0.09%
Value of Interest earned – Q2	£1,919	£1,567	+ £352
Oct to Dec 2009	0.38%	0.38%	0.00%
Value of Interest earned – Q3	£2,147	£2,147	£0
<b>Invesco Aim</b>			
April to June 2009	0.75%	0.49%	0.26%
Value of Interest earned - Q1	£3,006	£1,954	+ £1,052
July to Sept 2009	0.56%	0.41%	+0.15%
Value of Interest earned – Q2	£4,468	£3,296	+ £1,172

<b>Fund</b>	<b>Investment Return</b>	<b>LIBID Benchmark</b>	<b>Out/(Under) Performance</b>
Oct to Dec 2009	0.48%	0.38%	0.10%
Value of Interest earned – Q3	£4,230	£3,327	+ £903
<b>Prime Rate</b>			
April to June 2009	1.38%	0.49%	0.89%
Value of Interest earned – Q1	£15,997	£5,671	+ £10,326
July to Sept 2009	1.23%	0.41%	+0.82%
Value of Interest earned – Q2	£15,443	£5,129	+ £10,314
Oct to Dec 2009	1.07%	0.38%	0.69%
Value of Interest earned – Q3	£13,157	£4,694	+ £8,463

- 9.8 During the quarter ending December 2009, the policy was to continue using the Money Market Funds in preference to the Business Reserve Accounts for liquidity balances as the Money Market Funds were paying rates equal to or above the current Bank Rate. The comparable rates being offered by the Business Reserve Accounts were lower than the Money Market Fund rates because for the levels of investments being held in the accounts would not earn the top level, equivalent to bank rate. The Council has recently opened up a Money Market Fund Portal, which will be used for future trading in other new Money Market Funds.
- 9.9 The Council earned £19,534 interest on its Money Market Fund investments in the quarter ending 31<sup>st</sup> December 2009. The average principal maintained in the funds was £10,372,204.

### **Business Reserve Accounts**

- 9.10 The Council operates two Business Reserve accounts with Abbey National and Bank of Scotland. If sufficient balances are maintained these accounts offer a guaranteed rate of return equivalent to Bank Rate. However, because the Money Market Funds were offering rates above the Business Reserve Accounts for the levels of investments held, the Business Reserve Accounts were not used.
- 9.11 An analysis of the overall in house investments held by the Council at the end of December 2009 is shown below:  
(The previous quarter is shown for comparison)

<b>Type of Investment</b>	<b>Opening Balance Q3 As at 1<sup>st</sup> October 2009</b>	<b>Closing Balance Q3 As at 31<sup>st</sup> December 2009</b>
<b>In House</b>		
Money Markets	£29,500,000	£30,000,000
Money Market Funds	£8,036,000	£11,345,000
Business Reserve Accounts	£0	£0
<b>Total</b>	<b>£37,536,000</b>	<b>£41,345,000</b>

- 9.12 The above table shows how the Council cash balances increase on a cumulative basis throughout the year.
- 9.13 The original estimate of annual external investment interest for 2009/10 was £699,200 gross and the latest estimate is £729,900. This slight increase is mainly accounted for by an increase in balances due to slippage within the capital programme. In addition to this, the Council has received a further £599,300 from HMRC in respect of retrospective over payment of VAT.

## 10 **BORROWING**

- 10.1 During the quarter it was not necessary to undertake any Money Market borrowing to fund cashflow deficits, with any deficits being managed within the Councils £500,000 overdraft facility with HSBC. The interest rate on this facility is 1% above Bank Rate and is charged on the cleared balance at the end of each day when that balance is in debit i.e. overdrawn. In the October to December quarter interest amounting to £36 was paid on debit balances. This is normally offset by the interest earned at 1% below Bank Rate on the days when the end of day balance was in credit; however, with Bank Rate at 0.50% this is not applicable.

## 11 **EXTERNAL FUND MANAGERS**

- 11.1 Invesco Asset Management Ltd continues to act as the Council's external cash management agents and currently manage £5 million on our behalf.
- 11.2 Invesco's performance up to the end of December 2009 is shown below:

Quarter	Portfolio Net Return %	LIBID Benchmark %	Out/(Under) performance %
Oct to Dec 2009	0.23%	0.10%	+ 0.13%
Year to date	0.21%	0.29%	(0.08%)

- 11.3 Invesco has returned 0.23% for the quarter net of fees versus a benchmark of 0.10%, an outperformance of 0.13%. Given the very poor performance in the first quarter, the year to date results still reflect an under performance of (0.08%)
- 11.4 Invesco dealt in the gilt market quite frequently during the quarter. They were all at the short end of the market, the longest maturity being to March 2014. A number of trades were sold out fairly promptly, some making a small gain and other a small loss. The biggest investment was in the middle of December when approximately 20% of the portfolio was placed in a 4.25% 2011 gilt. Most of it was sold the next day for a small loss. Invesco finished the quarter with 20% of the portfolio held in gilts.
- 11.6 Invesco made several acquisitions in the CD market, confining themselves to purchasing one, two and three month maturities at yields ranging from 0.48% to 0.61%.
- 11.7 Throughout the quarter Invesco held a substantial proportion of the portfolio in cash, more than half, using the in house money market fund.

- 11.8 Invesco has managed a positive return for the third quarter of the year. They traded extensively in gilts, in the short end, and managed a small trading profit on their tactical trades.
- 11.9 At the end of December 2009, the value of the portfolio stood at £5,019,447 and the breakdown is shown in the table below:

Type of Investment	Amount
Gilts	£479,153
Certificates of Deposit	£3,500,847
Temporary Deposits	£1,039,447
<b>Total</b>	<b>£5,019,447</b>

- 11.10 It is estimated that the Invesco portfolio will earn £17,500 in interest for 2009/10 on the basis of its revised central case return of 0.35%. This is a reduction of £95,000 on the original budgets when Invesco's central rate forecast was 2.25%
- 11.11 The Council's Treasury Management Advisors, Sector, has analysed the performance of seven external fund managers, including Invesco. The annualised results up to the end of December show that all performed better than Invesco. This analysis also shows that Invesco do not achieve a level of return commensurate with the level of risk within the portfolio.
- 11.12 As detailed in full in the Quarter 2 report, the contract with Invesco as external fund managers to the Council is to be terminated. Formal notice has now been given to Invesco and the portfolio will be repaid with accrued interest earned to date by the end of the financial year. These funds will then be managed In House as a core investment.

## **12 PRUDENTIAL INDICATORS**

- 12.1 The 2009/10 Treasury Management Strategy included a number of Prudential Indicators within which the Council must operate. The two major ones are the Authorised Limit and Operational Boundary for borrowing purposes and it is confirmed that during the quarter neither indicator has been exceeded.