WARWICK DISTRICT COUNCIL	**Finance & Audit Scrutiny Committee - 14 February 2012**	**Agenda Item No. 5**

Title	**Treasury Management Activity Report for the period 1st October 2011 to 31st December 2011.**
For further information about this report please contact	Roger Wyton, Principal Accountant 01926 456801 roger.wyton@warwickdc.gov.uk
Wards of the District directly affected	All
Is the report private and confidential and not for publication by virtue of a paragraph of schedule 12A of the Local Government Act 1972, following the Local Government (Access to Information) (Variation) Order 2006	No
Date and meeting when issue was last considered and relevant minute number	n/a
Background Papers	Treasury Management File L2/9 Treasury Management Information via External Advisers, Brokers, External Investment Agents etc.

Contrary to the policy framework:	No
Contrary to the budgetary framework:	No
Key Decision?	No
Included within the Forward Plan? (If yes include reference number)	No
Equality & Sustainability Impact Assessment Undertaken	No – not relevant

Officer/Councillor Approval

Officer Approval	**Date**	**Name**
Chief Executive/Deputy Chief Executive	30/01/2012	Andy Jones
Head of Service	30/01/2012	Andy Jones
CMT	N/A	
Section 151 Officer	01/02/2012	Mike Snow
Monitoring Officer	N/A	
Finance	26/01/2012	Roger Wyton
Portfolio Holder(s)	N/A	

Consultation & Community Engagement

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 1st October 2011 to 31st December 2011.

2. RECOMMENDATIONS

2.1 That Finance and Audit Scrutiny Committee notes the contents of this report.

2.2 That Finance and Audit Scrutiny Committee indicates to Officers the frequency with which it wishes to receive in year performance reports.

3. REASONS FOR THE RECOMMENDATION

3.1 The Council's 2011/12 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. This is more often than the minimum half yearly report stipulated in the CIPFA Code of Practice and Members are requested to decide whether they wish to continue with quarterly performance reports or move to a half yearly basis.

3.2 Apart from 3.1 and paragraph 14.1, the rest of this report informs Members of past performance, hence Members are just asked to note the information contained within it.

4. POLICY FRAMEWORK

4.1 Treasury Management will support the Council in achieving its aims as set out in "Fit for the Future".

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 whilst ensuring the security of the capital. The Council is reliant upon interest received to help fund the services it provides. The current estimate for investment interest in 2011/12 compared with the original budget is shown in the table below:

	Latest 2011/12 Budget (Dec 11)	**Original 2011/12 Budget (Jan 11) £**
Gross Investment Interest	518,385	462,484
Less HRA allocation	162,691	146,300
Net interest to General Fund	**355,694**	**316,184**

5.2 When the 2011/12 original budget for investment interest was calculated in January 2011, it was expected that Bank Rate would begin to rise from its current 0.50% in the quarter ending December 2011. Sector's latest forecast as at October 2011 is that Bank Rate will not now rise until the quarter ending September 2013 (previously June 2012) which will not affect the latest budget shown above as it was prudently prepared on the basis of Bank Rate remaining at 0.50% throughout 2011/12. Offsetting this is the fact that the Council has increased balances available for investment during 2011/12, partly due to slippage in the 2010/11 capital programme and this has resulted in increased investment interest over the original.

6. ALTERNATIVE OPTION CONSIDERED

6.1 None.

7. ECONOMIC BACKGROUND

7.1 A detailed commentary by our Treasury Consultants, Sector, of the economic background surrounding this quarter appears as Appendix A.

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 31st December 2011. The Council's Treasury Management Advisors, Sector, provided the following forecast for future Bank Rates:

Sector's Bank Rate Forecasts:

Qtr ending	Now (Oct 11)	Dec 2011	Mar 2012	Jun 2012	Sep 2012	Dec 2012	Mar 2013	Jun 2013	Sep 2013	Dec 2013	Mar 2014	Jun 2014
Current Forecast, as at October 2011:												
Bank Rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%
Forecast, as at January 2011, (when Original Budgets were set):												
Bank Rate	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%	2.25%	2.75%	3.00%	3.25%	3.25%

During this quarter there was a marked deterioration in economic prospects affecting the US, UK and most significantly the Eurozone.

Recently we have seen some signs of improvement in the US economy but the expectation for UK economic growth continues to be weak and the economy may have already entered a technical recession (two quarters of negative growth). A major contributing factor to this is the continuing Eurozone Sovereign debt crisis which is inhibiting demand from one of the UK's major markets. Although Sector has not revised its Bank Rate forecast as yet it seems increasingly likely that Bank Rate will stay at 0.50% for much longer than the currently forecast September 2013, perhaps into 2016.

The forecast as at January 2011 is shown for comparison purposes as this forecast was used in calculating the original budgets.

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 2011/12 was approved by Council on 9th March 2011. This approved the current lending criteria which reflect 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 either from the residual impact of the past crisis in the banking sector or the potential issues arising from the current Eurozone debt crisis.

9 INVESTMENT PERFORMANCE

Money Market Investments

9.1. During 2011/12, the in house function has invested both cash flow driven and core cash funds in fixed term deposits in the Money Markets. The table below illustrates the performance of the in house function during this quarter for each category normally invested in:

Period	Investment Return (Annualised)	LIBID Benchmark (Annualised)	Out/(Under) performance
Up to 7 days			
April to June 2011	No investments made in this quarter.		
July to Sept 2011	No investments made in this quarter		
April to Sept 2011	No investments made in half year		
Oct to Dec 2011	No investments made in this quarter		
Year to Date	No investments made in year to date		
Over 7 days & Up to 3 Months			
April to June 2011	0.93%	0.49%	+0.44%
Value of Interest earned – Q1	£4,564	£2,402	+£2,162
July to Sept 2011	0.91%	0.63%	+0.28%
Value of Interest earned – Q2	£13,171	£9,163	+£4,008
April to Sept 2011	0.91%	0.56%	+0.35%
Value of Interest earned – half year	£17,735	£11,565	+£6,170
Oct to Dec 2011	0.97%	0.81%	+0.16%
Value of Interest earned – Q3	£36,772	£30,590	+£6,182
Year to Date	0.95%	0.71%	+0.24%
Value of Interest earned – Year to Date	£54,507	£42,155	+£12,352
Over 3 Months & Up to 6 Months			
April to June 2011	No investments made in this quarter.		
July to Sept 2011	No investments made in this quarter		
April to Sept 2011	No investments made in half year		
Oct to Dec 2011	1.26%	1.10%	+0.16%
Value of Interest earned – Q3	£6,283	£5,462	+£821
Year to Date	1.26%	1.10%	+0.16%
Value of Interest earned – Year to Date	£6,283	£5,462	+£821

Period	Investment Return (Annualised)	LIBID Benchmark (Annualised)	Out/(Under) performance
Over 6 Months to 364 days			
April to June 2011	1.71%	1.46%	+0.25%
Value of Interest earned – Q1	£68,255	£58,212	+£10,043
July to Sept 2011	1.14%	1.26%	-0.12%
Value of Interest earned – Q2	£20,997	£23,183	-£2,186
April to Sept 2011	1.53%	1.36%	+0.17%
Value of Interest earned – half year	£89,252	£81,395	+£7,857
Oct to Dec 2011	1.80%	1.48%	+0.32%
Value of Interest earned – Q3	£17,951	£14,804	+£3,147
Year to Date	1.57%	1.42%	+0.15%
Value of Interest earned – Year to Date	£107,203	£96,199	+£11,004
365 days and over			
April to June 2011	1.85%	1.40%	+0.45%
Value of Interest earned – Q1	£92,825	£70,067	+£22,758
July to Sept 2011	2.01%	1.50%	+0.51%
Value of Interest earned – Q2	£80.500	£60,036	+£20,464
April to Sept 2011	1.92%	1.45%	+0.47%
Value of Interest earned – half year	£173,325	£130,103	+£43,222
Oct to Dec 2011	No investments made in this quarter		
Year to Date	1.92%	1.45%	+0.47%
Value of Interest earned – Year to Date	£173,325	£130,103	+£43,222

9.2 Members will recall that they requested the Treasury function to investigate a more challenging alternative to the LIBID benchmarks shown above. Despite research and discussions with Sector no real alternative has been found and Sector has confirmed that in their view the LIBID benchmark is as good as any other. However, it is felt appropriate to add a margin of 0.0625% to the benchmark as some recognition of the need to provide a more competitive benchmark therefore all the LIBID rates in the table above and referred to below include this margin of 0.0625%.

9.3. During October to December, the majority of the Council’s cash flow investments were made into the Money Market Funds due to the short time span between the cash being received e.g. Council Tax and NNDR instalments and then paid out again e.g. County Council and Police Authority precepts. but 2 investments for cash flow purposes were made in the Over 7 Days and up to Three Months category during the quarter. In addition 10 maturing core investments were each re-invested for three months rather than being placed out for a further 364 days. This was on the advice of Sector who felt, and still do feel, that due to the ongoing problems in the Eurozone it is wise to limit investments to a maximum duration of three months until the situation resolves itself. In total, these investments produced an average return of 0.97% compared to the LIBID benchmark of 0.81% which is an amalgam of the 1 and 3 month LIBID rates. This out performance of 0.16% was achieved using a mix of building societies and banks such as Barclays and Santander. All the investments were for around three months in each case and when compared to the three month rate alone of 0.95% the out performance is 0.02%.

9.4 Before the advice to limit investments to a maximum duration of three months was received from Sector, an investment with Nationwide Building Society was made in the Over 3 months and Up to 6 Months category. This produced a return of 1.26% against the 3 and 6 month hybrid LIBID benchmark of 1.10% .The investment was for 182 days so when compared with the 6 month average LIBID rate alone of 1.24% there is an out performance of 0.02% against the 6 month LIBID rate

9.5 Again, before the advice to limit investments to a maximum duration of three months was received from Sector, another investment with Nationwide Building Society was made, this time for 364 days. This produced a return of 1.80% which when compared with the 364 day average LIBID rate of 1.73% shows an outperformance of 0.07% against the 364 day LIBID rate.

9.6 Given that the current Bank Rate is only 0.50% the level of outperformance achieved in this quarter continues to be satisfactory and it can be seen that adding 0.0625% to the benchmark does in fact make a more challenging target with our returns only just outperforming the enhanced benchmark.

Money Market Funds

9.7 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 together with a summary of the first half year performance is shown in the following table:

Fund	Investment Return (Annualised)	LIBID Benchmark (Annualised)	Out/(Under) Performance
Standard Life to 31st May 2011 (Deutsche from 1st June 2011)			
April to June 2011	0.61%	0.46%	+0.15%
Value of Interest earned – Q1	£4,454	£3,382	+£1,072
July to Sept 2011	N/A	N/A	N/A
April to Sept 2011	0.61%	0.46%	+0.15%
Value of Interest earned – half year	£4,454	£3,382	+£1,072
Oct to Dec 2011	N/A	N/A	N/A
Value of Interest earned – Q3	N/A	N/A	N/A
Year to Date	0.61%	0.46%	+0.15%
Value of Interest earned – Y to date	£4,454	£3,382	+£1,072

Fund	Investment Return (Annualised)	LIBID Benchmark (Annualised)	Out/(Under) Performance
Deutsche from 1st June 2011			
April to June 2011	0.66%	0.46%	+0.20%
Value of Interest earned – Q1	£2,954	£2,071	+£883
July to Sept 2011	0.66%	0.48%	+0.18%
Value of Interest earned – Q2	£6,637	£4,814	+£1,823
April to Sept 2011	0.66%	0.47%	+0.19%
Value of Interest earned – half year	£9,591	£6,885	+£2,706
Oct to Dec 2011	0.69%	0.56%	+0.13%
Value of Interest earned – Q3	£5,923	£4,784	+£1,139
Year to Date	0.67%	0.50%	+0.17%
Value of Interest earned – Year to Date	£15,514	£11,669	+£3,845
Invesco Aim			
April to June 2011	0.57%	0.46%	+0.11%
Value of Interest earned - Q1	£939	£767	+£172
July to Sept 2011	0.57%	0.48%	+0.09%
Value of Interest earned – Q2	£794	£668	+£126
April to Sept 2011	0.57%	0.47%	+0.10%
Value of Interest earned – half year	£1,733	£1,435	+£298
Oct to Dec 2011	0.63%	0.56%	+0.07%
Value of Interest earned – Q3	£298	£264	+£34
Year to Date	0.59%	0.50%	+0.09%
Value of Interest earned – Year to Date	£2,031	£1,699	+£332

Fund	Investment Return (Annualised)	LIBID Benchmark (Annualised)	Out/(Under) Performance
Prime Rate			
April to June 2011	0.83%	0.46%	+0.37%
Value of Interest earned – Q1	£12,239	£6,820	+£5,419
July to Sept 2011	0.86%	0.48%	+0.38%
Value of Interest earned – Q2	£12,620	£7,070	+£5,550
April to Sept 2011	0.85%	0.47%	+0.38%
Value of Interest earned – half year	£24,859	£13,890	+£10,969
Oct to Dec 2011	0.94%	0.56%	+0.38%
Value of Interest earned – Q3	£10,672	£6,391	+£4,281
Year to Date	0.88%	0.50%	+0.38%
Value of Interest earned – Year to Date	+£35,531	+£20,281	+£15,250
Ignis			
April to June 2011	N/A	N/A	N/A
July to Sept 2011	N/A	N/A	N/A
Oct to Dec 2011	0.87%	0.56%	+0.31%
Value of Interest earned – Q3	£6,513	£4,188	+£2,325
Year to Date	0.87%	0.56%	+0.31%
Value of Interest earned – Year to Date	£6,513	£4,188	+£2,325
Goldman Sachs			
April to June 2011	N/A	N/A	N/A
July to Sept 2011	N/A	N/A	N/A
Oct to Dec 2011	0.61%	0.56%	+0.05%
Value of Interest earned – Q3	£564	£515	+£49
Year to Date	0.61%	0.56%	+0.05%
Value of Interest earned – Year to Date	£564	£515	+£49

9.8 As referred to in paragraph 9.3 above, during the quarter ending December 2011 the majority of the Council's cash flow investments were into the Money Market Funds and the policy of using these funds in preference to the Business Reserve Accounts for liquidity balances was continued 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 we would not earn the top level, equivalent to Bank Rate or slightly higher. The Council opened up two new Money Market Funds, Ignis and Goldman Sachs, during the quarter and utilised them both.

9.9 As with the Money market investments in paragraph 9.1, the LIBID benchmark which in this case is the 7 day rate has been increased by a margin of 0.0625% and it can be seen from the table above that the out performance of the benchmark continues to be satisfactory with the two new funds performing in line with expectations. The Council continued to concentrate its investments in the three highest performing funds Prime Rate, Ignis and Deutsche although on occasions it was necessary to utilise the Invesco Aim and Goldman Sachs funds due to counterparty limits on the other funds being reached..

9.10 On an annualised basis, the Council will earn £23,970 interest on its Money Market Fund investments in the quarter ending 31st December 2011. The average balance in the funds for the quarter was £14,713,873.

Business Reserve Accounts

9.11 The Council operates two Business Reserve accounts with Santander and Lloyds Banking Group. If sufficient balances are maintained these accounts offer a guaranteed rate of return equivalent to Bank Rate or slightly higher. 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.

9.12 The following table brings together the investments made in the various investment vehicles so far this year to give an overall picture of the investment return to date:-

Investment Vehicle	Investment Return (Annualised) £	LIBID Benchmark (Annualised) £	Out/(Under) Performance £
Money Markets	341,318	273,919	+67,399
Money Market Funds	64,607	41,734	+22,873
Total	**405,925**	**315,653**	**+90,272**

The original estimate of annual external investment interest for 2011/12 was £462,484 gross and this was revised in December to £518,385, the additional amount being partly due to increased balances available for investment resulting from slippage in the capital programmes. It should be noted that the total investment return of £405,925 shown in the table above does not correspond to the £518,385 as the £405,925 represents the investments made in this year to date i.e.there will be further investments to be made during the final quarter of the year. Also, the £405,925 is an annualised figure and will include interest relating to 2012/13 so in order to arrive at the £518,385 it is necessary to strip out the interest relating to 2011/12 from the £405,925 and any investments yet to be made in 2011/12 and add to it the interest relating to 2011/12 from 2010/11 investments maturing in 2011/12.

9.13 An analysis of the overall in house investments held by the Council at the end of December 2011 is shown below:

(The previous quarter is shown for comparison)

Type of Investment	Closing Balance Q2 As at 30th Sept 2011	Closing Balance Q3 As at 31st Dec 2011
	£	£
Money Markets	34,000,000	35,000,000
Money Market Funds	5,847,000	11,727,000
Business Reserve Accounts	0	0
Total	**39,847,000**	**46,727,000**

10. **COUNTERPARTY CREDIT RATINGS**

10.1 Except for an appendix to the Treasury Management Strategy Plan presented to the Executive in February each year, an analysis of the credit ratings enjoyed by our various counterparties with whom we have invested in recent times has never been reported regularly to Members. In these heightened times of concern over the Eurozone crisis and its potential impact on UK banks it is felt appropriate to provide such a regular update listing the investments made in the quarter and the credit ratings applicable to the counterparty at the point at which the investment was made and this is shown in the table below:-

Counterparty	Investment Amount £	Credit Rating			
		Long Term	Short Term	Individual	Support
Banks					
WDC Minimum	(Fitch)	**A+**	**F1**	**B/C**	**1**
Barclays Bank	£4,000,000	AA-	F1+	B	1
Santander	£1,000,000	A+	F1	B	1
Rated Building Societies					
WDC Minimum	(Fitch)	**A+**	**F1**	**N/A**	**N/A**
Nationwide	£3,000,000	AA-	F1+	B	1
Unrated Building Societies					
WDC Minimum	**Must be in Top 20 ranked by Asset Value**				
Furness	£1,000,000	Ranked 16			
Manchester	£1,000,000	Ranked 15			
Newcastle	£1,000,000	Ranked 8			
West Bromwich	£1,000,000	Ranked 6			
Hinckley & Rugby	£1,000,000	Ranked 20			
Principality	£1,000,000	Ranked 7			
Nottingham	£1,000,000	Ranked 9			
Skipton	£1,000,000	Ranked 4			
MoneyMarket Funds (Investment amount is average principal in fund during the quarter)					
WDC Minimum	Fitch AAA & Volatility rating VR1+ or S & P AAAm or Moodys AAA & Volatility Rating MR1+				
Deutsche	£3,389,000	Fund retained its rating throughout quarter			
Invesco Aim	£187,000	Fund retained its rating throughout quarter			
Prime Rate	£4,528,000	Fund retained its rating throughout quarter			
Ignis	£5,151,000	Fund retained its rating throughout quarter			
Goldman Sachs	£1,459,000	Fund retained its rating throughout quarter			

10.2 It can be seen that both banks utilised during this quarter either matched or exceeded the minimum WDC credit rating criteria as did the one rated building society used. With regard to the unrated building societies, all were within the top 20 ranked by asset value with a minimum asset value of £644m (Furness) which is comfortably in excess of the minimum floor of £500m being recommended for 2012/13 within the 2012/13 Annual Investment Strategy to be presented to Council in February. In addition, the investments were limited to £1m apiece and for a maximum of 3 months in order to further reduce credit and counterparty risk.

11. **BENCHMARKING**

11.1 At its last meeting, members of this Committee asked whether an alternative benchmark to the LIBID rates could be found which would prove more challenging. Despite research and discussions with Sector, it appears no real alternative benchmark can be found. However, it is felt appropriate to make the benchmark 0.0625% <u>over</u> LIBID in order to make it more of a challenge.

11.2 With regard to the Sector Treasury Management Benchmarking Club, the Council is part of a local group comprising both District and County Councils and analysis of the results for the December quarter show that the Councils weighted average rate of return on its investments made in the December quarter at 1.23% was in line with Sector's model portfolio rate of return based on the risk in our portfolio which was 1.26% and considerably above the group's rate of return which was 1.08%. Further analysis indicates that the groups relatively low rate of return was in part due to significant amounts of investments, particularly by the County Councils, being placed with the Governments overnight and short term Debt Management Office (DMO) facility (in one instance 100% of a County Council's investments were with the DMO) which offers high security but at the expense of significantly lower interest rates than could be obtained from investing in Money Market Funds thus depressing the groups weighted average rate of return. Money Market Funds are themselves of equal security being AAA rated and were widely used by this Council during the December quarter thus contributing to the out performance.

11.3 A further contributing factor to the outperformance seems to be the fact that other members of the club are investing a significant element of their portfolio's in short duration assets of less than 1 month. Whilst this undoubtedly reduces the risk that a counterparty may default during the duration of an investment it does lessen the ability to maximise investment returns whilst still adequately protecting the security of the investment. Sector's current advice is to invest for up to three months which still limits the risk of default whilst providing a reasonable rate of return which is the approach that the Treasury team took during the December quarter and are continuing to take.

12. BORROWING

12.1 During the quarter it was not necessary to undertake any Money Market borrowing to fund cashflow deficits, with any deficits being managed within the Council's £100,000 overdraft facility with HSBC. The interest rate on this facility is 2% 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 December

2011 quarter £6.12 was paid in overdraft interest. Overdraft interest 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.

13 PRUDENTIAL INDICATORS

13.1 The 2011/12 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. A report has been submitted to the February Executive and Council recommending that both indicators be increased to take account of the HRA Self Financing debt settlement of approx. £140m which will take place on 28th March 2012.

14. FREQUENCY OF REPORTING

14.1 As part of the Council's Fit for the Future programme, the Treasury Management function underwent a systems intervention during the 2011 Summer and Autumn. Various minor amendments to record keeping were made but the intervention highlighted that the quarterly progress reports submitted to this Committee were more frequent than strictly necessary, the minimum being one half yearly report under the CIPFA Treasury Management Code of Practice together with an Annual report within 6 months of the end of the year to which it relates. Bearing in mind that the half yearly report is the minimum requirement, Members are asked to decide how often they wish to receive Treasury Management progress reports during 2012/13.

APPENDIX A

1. SECTOR COMMENTARY ON THE CURRENT ECONOMIC BACKGROUND.

1.1 Activity indicators suggested that the economic recovery ground to a complete halt in the third quarter and output may even have contracted. The weighted output balance of the CIPS/Markit surveys in October fell to a level that has been consistent in the past with a contraction in GDP. The output balance then broadly held at that level in November.

1.2 The CIPS surveys exclude the retail sector and the latest news from the high street has been poor, reflecting the pressures on households' finances. According to the official figures, retail sales volumes (ex. petrol) rose by 0.9% m/m in October but then fell by 0.7% in November, despite deep discounts offered by retailers. Timelier survey and anecdotal evidence suggests that, by and large, spending was weaker than usual in December.

1.3 Conditions in the labour market have also continued to deteriorate, albeit at a slower pace than in previous months. The Labour Force Survey measure of employment fell by 63,000 in the three months to October, a slower pace of deterioration than seen in the second quarter. The number of employees plummeted by 252,000 – but this was partly offset by a 166,000 rise in self-employment. Rises in the timelier claimant count measure of unemployment also became more modest – it increased by 'just' 2,500 on the previous month in October and 3,000 in November. Despite this moderating trend, employment surveys have continued to point to further job losses ahead.

1.4 The housing market has continued to recover, albeit slowly. The number of mortgage approvals for new house purchase rose from 51,200 in September to 52,900 in November. And according to the Nationwide, house prices were 0.6% higher in December than they were in September. Nonetheless, banks began the process of passing on the rise in their wholesale funding costs, reflecting the adverse effects of the euro-zone debt crisis, to consumers during the quarter.

1.5 The latest trade data tentatively suggested that net trade was on course to make a positive contribution to GDP growth in the third quarter. The trade in goods and services deficit narrowed from £4.3bn in September to £1.6bn in October (although the monthly deficit figures have been volatile recently). Some survey measures have also pointed to a recent pick-up in demand for exports as the new export orders balance of the CIPS manufacturing survey rose from 49.0 in November to 53.5 in December. At that level, it points to a quarterly rise in the volume of manufactured goods exports of around 2%.

1.6 Despite much weaker than expected GDP growth, the latest public finance figures showed that borrowing is coming in comfortably below last year's totals. Spending growth has slowed, while growth in tax receipts is still holding up reasonably well. And if the trend so far this fiscal year is sustained, borrowing will total about £122bn in 2011/12, equal to what the Office for Budget Responsibility (OBR) was forecasting until it revised its forecast to £127bn in its Economic and Fiscal Outlook that accompanied the Chancellor's Autumn Statement. The OBR also revised up its forecasts for borrowing in future years to reflect its much weaker expectations for GDP growth.

1.7 Inflation fell in the third quarter with CPI inflation falling from its recent peak of 5.2% in September to 5.0% in October and 4.8% in November. It probably fell further in December as past rises in energy prices a year ago dropped out of the annual comparison. Inflation remained on track to fall further in the coming months. Oil prices, for example, remained largely range-bound between $105pb and $115pb, while petrol prices began to fall. Meanwhile, the continued weakness of indicators of money supply growth and firms' pricing intentions, as well as the still large degree of spare capacity in the economy, suggested that underlying inflationary pressures are still very weak.

1.8 Granted, measures of inflation expectations remained quite high – the Bank of England's measure of households' inflation expectations for the year ahead only edged down from 4.2% to 4.1% in Q3. But considerable slack in the labour market should continue to prevent the translation of these expectations into stronger earnings growth. Indeed, the annual rate of average earnings growth including bonuses rose was just 2% in October (a slight rise from 1.9% in September). Real pay growth has therefore remained negative.

1.9 The MPC restarted quantitative easing (QE) in October and announced £75bn of additional gilt purchases would be completed by February. The MPC also looked primed to sanction further purchases in Q4. The November Inflation Report forecast projected CPI inflation to be well below the 2% target in two years' time, while speeches by certain members of the Committee (such as Martin Weale and Paul Fisher) suggested that they thought there was a strong case for more purchases.

2.0 Largely reflecting this dovish stance, markets expectations for official interest rates continued to fall during Q3, helping government bond yields to drop to new record lows (the 10-year gilt yield fell from 2.43% to 2% at the end of the year). The drop may also have reflected growing demand for safe-havens – while bond markets thought that default risk on UK government bonds had grown during the quarter, they viewed that risk to be lower than in many other major economies, including Germany.

2.1 In contrast to the UK, the economic data improved in the US in Q3. The manufacturing ISM strengthened in November and December to a level consistent in the past with annual GDP growth of 2.5% to 3.0%. Non-farm payrolls also increased by 112,000 in October and 100,000 in November.

2.2 In the euro-zone, policymakers made little progress to deal with the region's debt crisis. The economic data in the euro-zone also continued to weaken – while the composite PMI rose in November in December, it remained below the theoretical "no-change" level of 50 and on past form was consistent with quarterly falls in GDP of almost 1%. A deep recession in the euro-zone remains a key risk to the outlook for the UK economy.