Report No. RES12014	London Borough of Bromley	Agenda Item No.

PART 1 - PUBLIC

Decision Maker:	**Executive and Resources PDS Committee and Resources Portfolio Holder**		
Date:	**25th January 2012**		
Decision Type:	Non-Urgent	Non-Executive	Non-Key
Title:	**TREASURY MANAGEMENT - PERFORMANCE Q3 2011/12**		
Contact Officer:	Martin Reeves, Principal Accountant (Technical & Control) Tel: 020 8313 4291 E-mail: martin.reeves@bromley.gov.uk		
Chief Officer:	Director of Resources		
Ward:	All		

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1. Reason for report

1.1 This report summarises treasury management activity during the quarter ended 31st December 2011 and the period 1st April 2011 to 31st December 2011 and updates Members on the Council's investment with Heritable Bank (paragraph 3.12).

RECOMMENDATION(S)

2.1 The PDS Committee and the Portfolio Holder are asked to note the report.

Corporate Policy

1. Policy Status: Existing policy. To maintain appropriate levels of risk, particularly security and liquidity, whilst seeking to achieve the highest rate of return on investments.

2. BBB Priority: Excellent Council.

Financial

1. Cost of proposal: N/A

2. Ongoing costs: N/A.

3. Budget head/performance centre: Interest on balances

4. Total current budget for this head: £2.691m (net) in 2011/12; surplus of £300k currently forecast plus £700k from part-reversal of Icelandic Bank impairment

5. Source of funding: Net investment income

Staff

1. Number of staff (current and additional): 0.4 fte

2. If from existing staff resources, number of staff hours:

Legal

1. Legal Requirement: Non-statutory - Government guidance.

2. Call-in: Call-in is applicable

Customer Impact

1. Estimated number of users/beneficiaries (current and projected): n/a

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Ward Councillor Views

1. Have Ward Councillors been asked for comments? N/A.

2. Summary of Ward Councillors comments:

3. COMMENTARY

General

3.1 Under the requirements of the CIPFA Code of Practice on Treasury Management, the Council is required, as a minimum, to approve an annual treasury strategy in advance of the year, a mid-year review report and an annual report following the year describing the activity compared to the strategy. In practice, the Finance Director has reported quarterly on treasury management activity for many years, as well as reporting the annual strategy before the year and the annual report after the year-end. The mid-year review for 2011/12 was considered by the PDS Committee on 14th November 2011 and will be reported to the Council meeting on 20th February. This report includes details of treasury management activity during the quarter ended 31st December 2011 and the period 1st April 2011 to 31st December 2011. The 2012/13 annual strategy, including the MRP (Minimum Revenue Provision) Policy Statement and prudential indicators, is reported elsewhere on the agenda.

Treasury Performance in the quarter ended 31st December 2011

3.2 **Borrowing:** The Council's healthy cashflow position has continued into 2011/12, as a result of which no borrowing has been required during the first three quarters of the year. In 2009/10, only four loans were taken out to cover short-term cashflow shortages and, in 2010/11, only one small overnight loan (for £800k) was taken out (in March 2011).

3.3 **Investments:** The following table sets out details of investment activity during the latest quarter:-

Main investment portfolio	**Deposits £m**	**Ave. Rate %**
Balance of "core" investments as at 30/09/11	162.5	1.96
New investments made in Q3 2011/12	35.0	1.54
Investments redeemed in Q3 2011/12	-35.0	1.48
Total "Core" Investments 31/12/11	162.5	2.00
Money Market Funds/Instant & 35-day Access	28.0	
Total Investments as at 31/12/11	**190.5**	

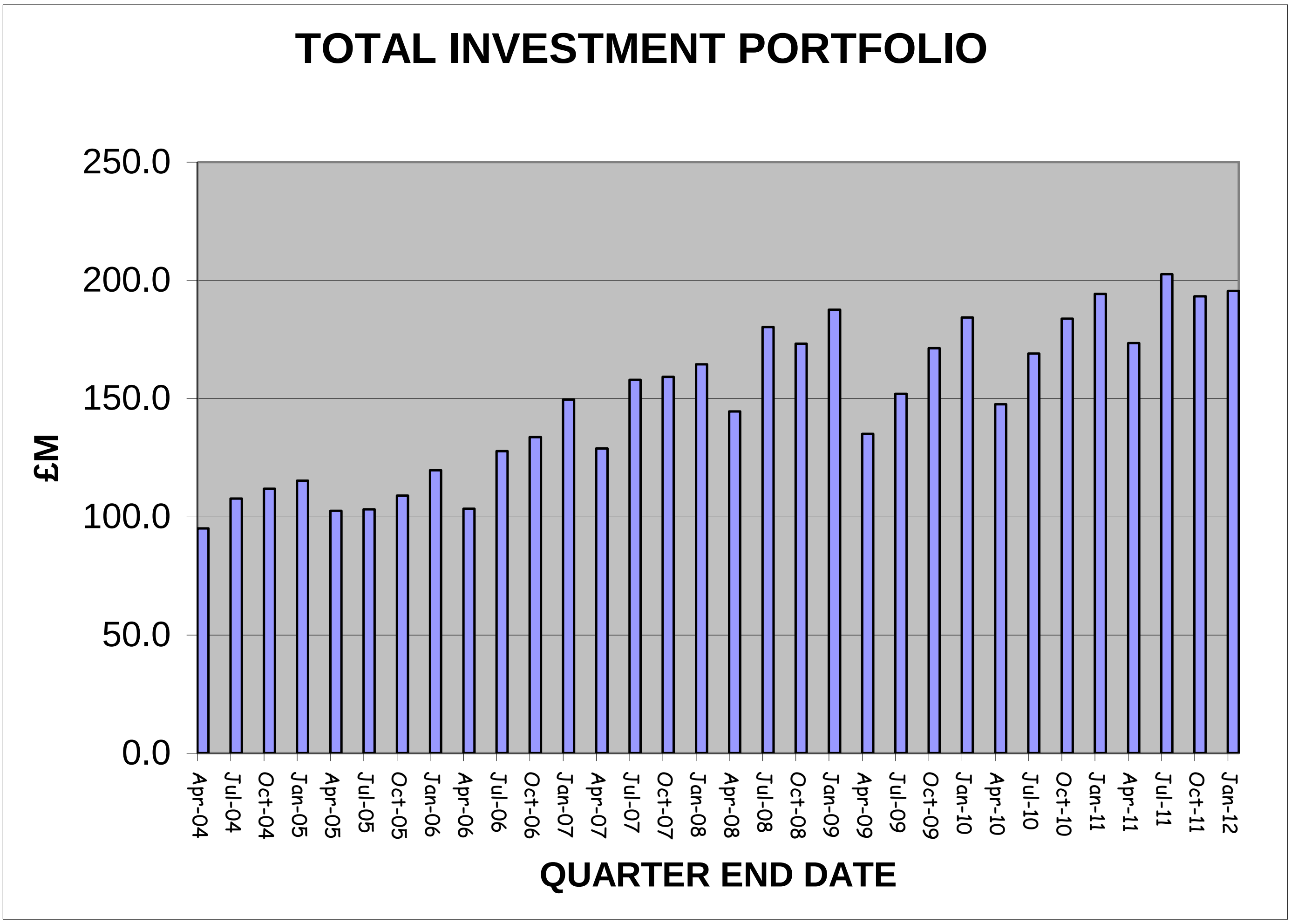
3.4 Details of the outstanding investments at 31st December 2011 are shown in maturity date order in Appendix 1 and by individual counterparty in Appendix 2. The average return on all new "core" investments during the December quarter was 1.54% which may be compared with the average 3 month LIBID rate of 0.89% and the average 7 day rate of 0.50%. The average return on new investments placed in the period 1st April to 31st December 2011 was 1.62% compared to the average 3 month rate of 0.78% and the average 7 day rate of 0.48%.

3.5 Base rate has now been 0.5% since March 2009 and the latest forecast by Sector is for it to remain at that level until the summer of 2013, although this date keeps moving back. Recent ratings downgrades have resulted in a number of our eligible UK bank counterparties, Barclays, Santander, Nationwide and Clydesdale, either having their limits, both monetary and time, being reduced or, in the case of Clydesdale, being removed from the list completely. This is discussed in more detail in paragraph 3.15, but it has seriously limited our options with regard to the reinvestment of maturing deposits and, in the Annual Strategy report elsewhere on the agenda, changes are proposed to the counterparty eligibility criteria to enable us to retain some options and a degree of flexibility with regard to future investments. Most of the institutions that do remain on our lending list at this time are offering around 1.00% for 3 months up to 1.85% for 1 year, both of which have risen slightly in the last quarter. Better rates (around 1.40% for 3 months, 2.50% for a year and 3.10% for two years) are available from Lloyds TSB, while Santander are currently offering 1.38% and 2.25% for 3 months and 1 year respectively.

3.6 In February 2010, the Portfolio Holder agreed changes to the Council's investment strategy to allow investment for up to 2 years with the largely-government owned Lloyds TSB and Royal Bank of Scotland (since November 2008, following the Icelandic banking crash, investments had been limited to a maximum period of 1 year). The "core" investments placed during the first three quarters of 2011/12 were in the main placed for between 6 months and a year, although three were placed for two years with Lloyds and RBS in order to take advantage of higher rates on offer (up to 2.80%) and the security offered by the (part-)government ownership. In view of continuing uncertainties in world financial markets and in line with external advice, investments have been kept shorter since September, having been mainly placed for 3 or 6 months (1 year with the part-nationalised banks). A proposal to the Executive on 19th October to increase the lending limit for the two part-nationalised banks from £40m to £60m was not supported at this stage and the Finance Director will continue to monitor rates and counterparty quality, as well as taking external advice, prior to any investment decisions.

3.7 The credit ratings changes since 2008 have resulted in the removal of many of our established counterparties from our lending list and, since then, it has been difficult to identify institutions to place money with. As a result, much greater use has been made of Money Market Funds, which provide a safe haven and instant access, but offer considerably lower interest rates. Information on Money Market Fund investments is provided in paragraph 3.9.

3.8 The graph below shows total investments at quarter-end dates back to 1st April 2004 and shows how available funds have increased steadily over the years, largely due to increased and earlier government funding. This has been a significant contributor to the over-achievement of investment income against budget in recent years, although this has now been fully factored into the revenue budget.



Other accounts

3.9 Money Market Funds

The Council currently has 5 Money Market Fund accounts, with Fidelity, Prime Rate, Insight, Blackrock and Ignis. In common with market rates for fixed-term investments, interest rates on money market funds have also fallen considerably in recent years, although they have recovered slightly in recent months. The Prime Rate fund currently offers the best rate (0.93%), which is only slightly below the 3-month rate offered by many of our eligible UK banks and building societies. The balances are likely to reduce to zero by the end of March as funds will be required to cover diminishing Council Tax receipts in the final quarter.

Money Market Fund	Date Account Opened	Ave. Rate 2011/12 (to 31/12/11) %	Ave. Daily Balance 2011/12 £m	Actual Balance 31/12/11 £m	Current Balance 05/01/12 £m	Current Rate 05/01/12 %
Prime Rate	15/06/09	0.83	10.5	13.0	15.0	0.93
Ignis	25/01/10	0.80	8.4	-	14.9	0.87
Insight	03/07/09	0.67	1.5	-	-	0.78
Blackrock	16/09/09	-	-	-	-	0.46
Fidelity	20/11/02	-	-	-	-	0.67

3.10 Notice Accounts

In April 2011, the Council placed £15m in a 35-day notice account with Svenska Handelsbanken (Sweden). The total of £15m is still currently invested at a rate of 0.85% and the average daily balance in the first three quarters of 2011/12 was £10.5m. It is likely that notice will be given for withdrawal in March to cover reduced Council Tax income towards the end of the year.

3.11 External Cash Management

External cash managers, Tradition UK Ltd, currently manage £20m of our cash portfolio and provide useful advice and information on treasury management matters. In the first three quarters of 2011/12, Tradition UK achieved a return of 1.67% (mainly bolstered by the two longer term investments placed in May and August (see table below)). Tradition UK, like the Council's in-house team, have been constrained by strategy changes approved after the Icelandic Bank crisis and by recent ratings downgrades. Details of externally managed funds placed on deposit as at the time of writing this report are shown below.

Sum	Start Date	Maturity	Period	Rate
Tradition UK				
£2.5m	17/05/11	22/03/12	10 months	1.25%
£5m	10/06/11	22/03/12	9.5 months	1.23%
£5m	12/08/11	27/03/12	7.5 months	1.20%
£2.5m	17/05/11	27/07/12	14.5 months	2.65%
£5m	17/08/11	16/08/13	2 years	2.80%

3.12 Investment with Heritable Bank

Members will be aware from regular updates to the Resources Portfolio Holder and the Executive that the Council had £5m invested with the Heritable Bank, a UK subsidiary of the Icelandic bank, Landsbanki, when it was placed in administration in early-October 2008 at which time our investment was, and still is, frozen. The latest estimate given by the administrators, Ernst & Young, late in September 2011 indicates a likely return of between 86% and 90% of our claim. This represents a significant improvement on the previous estimate of between 79% and 85% and Council officers and our external advisers remain hopeful of an even better result. An initial dividend was paid to the Council in July 2009 and, since then, a further eight dividends have been received. To date, 64.6% of our total claim (£3,286k) has been returned to us, leaving a balance of £1,801k (35.4%).

For information, the claim we were obliged to submit consisted of the principal sum (£5m) plus interest due to the date on which Heritable was placed in administration (around £87,000). We were not able to lodge a claim for the full amount of interest (£321,000) that would have been due at the original investment maturity date (29/6/09). In accordance with proper accounting practice and guidance from CIPFA, we made provision in our 2008/09 accounts for an impairment loss of £1.64m and met this from the General Fund in the year. In line with revised guidance from CIPFA relating to the 2009/10 accounts, we were able to reduce the impairment by £300k and this sum was credited to the General Fund. The latest improved recovery estimate of between 86% and 90% would potentially enable us to reverse a further £0.7m of the impairment, which would be credited to the General Fund as additional interest income in 2011/12. This would leave a provision for a net loss of £640k in the accounts, which will potentially reduce or clear depending on the size of the final settlement sum.

Regulatory Framework, Risk and Performance

3.13 The Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
- The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions were made in 2009/10);
- Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act;
- The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;
- The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;
- Under the Act the CLG has issued Investment Guidance to structure and regulate the Council's investment activities;
- Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices. Guidance on Minimum Revenue Provision was issued under this section on 8th November 2007.

3.14 The Council has complied with all of the above relevant statutory and regulatory requirements which limit the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach.

4. POLICY IMPLICATIONS

4.1 In line with government guidance, the Council's policy is to seek to achieve the highest rate of return on investments whilst maintaining appropriate levels of risk, particularly security and liquidity.

5. FINANCIAL IMPLICATIONS

5.1 An average of 1.5% was assumed for the interest rate on new investments in the 2011/12 revenue budget (£2.69m), in line with interest rate forecasts provided in January 2011 by the Council's external treasury advisers. The average rate obtained on all new investments placed since the budget was agreed is slightly above this at around 1.60%. Rates are still expected to rise, but the expected start of the rise has been put back to the summer of 2013 and may well slip back even further. The latest financial forecast assumes 1.5% in 2012/13, 1.50% in 2013/14, 2.0% in 2014/15 and 2.5% in 2015/16. A variation of 0.25% in these assumptions would result in a variation in interest earnings of around £400k pa from 2012/13. The latest forecast for 2011/12 is for a total surplus of £1.0m, comprising £0.3m from general investments and £0.7m as a result of the recent improvement in the Heritable administrator's recovery estimate (see paragraph 3.11).

Non-Applicable Sections:	Legal and Personnel Implications
Background Documents: (Access via Contact Officer)	CIPFA Code of Practice on Treasury Management CIPFA Prudential Code for Capital Finance in Local Authorities CLG Guidance on Investments External advice from Sector Treasury Services