

Item No:	Classification: Open	Date: 29 th July 2003	Meeting Name: EXECUTIVE
Report title:		Treasury Management – Annual Report 2002/03	
Wards or Groups affected:		All	
From:		Chief Finance Officer	

RECOMMENDATIONS

1. The Executive is asked to note the action taken in 2002/03 to manage the Council's long term debt and cash.

EXECUTIVE SUMMARY

2. This report sets out the 2002/03 borrowing and cash management activity carried out by the Chief Finance Officer under borrowing limits and policy established by Council.
3. The debt the Council had to fund past investment in capital was reduced by £46.6m. The reduction was met from earmarked revenue resources, earmarked asset sales and a £10m contribution from Right to Buy receipts. This brought the level of debt down to £720m as at 31st March 2003, within levels supported by the Government. The £10m contribution helps reduce the long run revenue cost of debt.
4. No new borrowing was carried out and the Council had no variable or short term debt. All debt was within limits determined by the Council for the year (overall limit £920m; short term limit £180m; variable limit 30%).
5. The average rate of interest on debt is 9.2%, reflecting the period in the 1970's and 1980's when high rates coincided with high capital expenditure. Although the rate is high relative to current rates for new loans (c.4.5%), Government support ensures that relatively little interest cost falls on local taxation and rents.
6. The average cash balance for 2002/03 was £134m, held in deposits with large high rated banks, building societies and the Government deposit facility to preserve the capital base. The interest earned for the year was £5.76m, in line with money market movements.
7. Cash management is carried out by in-house staff and external managers. Up to October 2002, the Council had two external managers. It now has just one manager (Invesco Asset Management Ltd). The contract with Dresdner RCM Global Investors UK Ltd was terminated following their withdrawal from the local authority cash management business and the money brought in-house.

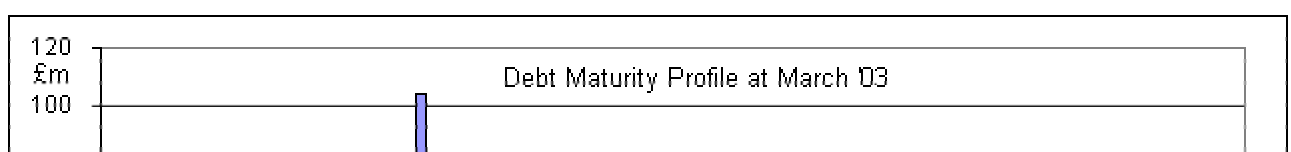
BACKGROUND

8. The Council's borrowing and cash are managed in a framework set out in the Treasury Management Code of Practice issued by the Chartered Institute of Public Finance and Accountancy. Under the framework, which is supported by a Treasury Management Manual, the Chief Finance Officer reports on borrowing and cash management strategy and activity. This is a report about activity in 2002/03, strategy on which was reported on 25th February 2002. The Council is responsible for determining borrowing limits, within which all day to day activities are the responsibility of the Chief Finance Officer.

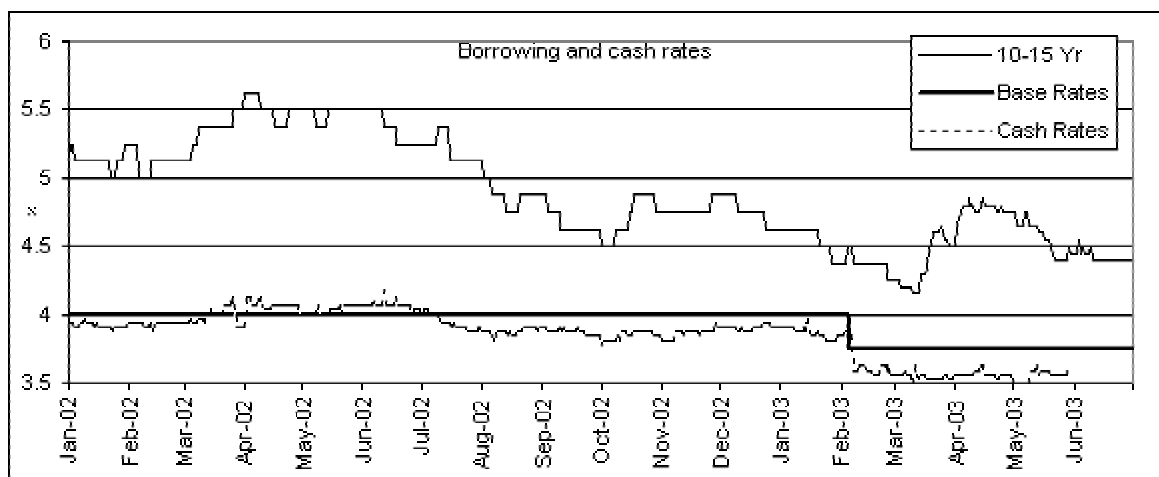
KEY ISSUES FOR CONSIDERATION

Borrowing 2002/03

9. Council borrowing arises from its historical investment in Housing and General Fund capital programmes. At the start of 2002/03 Council borrowing stood at £766.6m, primarily owed to the Public Works Loans Board, the local authority lending arm of the Government. During the year £46.6m loans were paid off which left £720m remaining at 31st March 2003. The repayment attracted a premium of £3m. The Council had no variable rate or short term debt and no other debt management activity was carried out, so the Council was within the three borrowing limits determined for the year (overall limit £920m; short term limit £180m; variable limit 30%).
10. The average rate of interest on debt is 9.2%, high relative to current rates (c.4.5%) for new loans, and reflects the period in the 1970's and 1980's when borrowing to support high investment in the Housing and General Fund capital programme coincided with high interest rates. However with 90% of the interest cost supported through Housing subsidy and the remainder partially supported in Formulae Grant, only a small proportion of interest cost falls directly on local taxation or rents. Premiums, which arise from debt repayment, also attract 90% subsidy, which is payable in instalments running over several years.
11. The £46.6m repayment was met from earmarked revenue resources and asset sales as envisaged under the strategy. This ensured that average debt remained within credit calculation used in support calculations and minimised unsupported costs. (The average debt was £728m whilst the credit calculation was £730m). As in the previous years, loan repayments from Right to Buy proceeds were raised by £10m to help reduce future revenue contributions to debt.
12. The maturity profile of debt following the repayments is set out in the chart below. There are no maturities over the next few years as loans which had fallen for repayment in those year have been paid off.



13. All debt is at fixed rates of interest ranging between 4.25% and 11.5%. There is no variable rate debt. The interest paid in 2002/03 was £67.2M (£71.2m 2001/02).
14. Interest rates prevailing in 2002/03 were much lower than the average rate of interest on Council debt 9.2%; refer chart below. It was possible to reduce this average by replacing high coupon loans with new loans at lower rates, but this was ruled out as an option under the strategy as premiums and funding costs remained high, despite support.



Borrowing 2003/04 – Update

15. In April 2003, £43m debt was paid off at a premium of £12.4m. This will help ensure debt remains within supported levels. As in 2002/03, the repayment will be met from earmarked revenue resources and asset sales. Additionally it will be possible to meet unsupported premiums from capital receipts to reduce burden on revenue budgets.
16. A code of practice (The Prudential Code) is being developed by the Chartered Institute of Public Finance and Accountancy on capital finance. The Code is in draft and is being supported by the Government. When it is finalised and comes into effect (which could be as early as 2004/05), local authorities will be required under the current draft, to publish three year estimates of local taxation and rents, plus plans and indicators on capital programme and borrowings. The Code aims to support Government plans for new freedoms to borrow for capital investment, whilst protecting local taxation and rents. This could generate additional capital expenditure, provided revenue savings to meet debt cost are found from council tax or rent increases. Deciding to raise council tax to enhance capital spending is one of the choices that members will have under new freedoms. The Council has begun its annual

rolling three year business planning processes. The results from these will inform decisions required under the code when it is finalised.

Cash Management 2002/03

17. The average cash balance for 2002/03 was £134m. Daily balances fluctuate according to movements in receipts and payments across the Council. The balance reached a low of £109m in June 2002 and a high of £170m in March 2003. The balance is invested in deposits with large high rated banks building societies and the Government to earn interest, which reduces the burden on local taxation and rents.
18. The cash is managed by in-house staff and external managers. Up to October 2002, the Council had two managers (Invesco Asset Management Ltd and Dresdner RCM Global Investors UK Ltd). In October the contract with Dresdner RCM was terminated, following their decision to withdraw from the local authority cash management business, and the money brought back in-house. The in-house operation has been enhanced since the Government made available its deposit facility with the Debt Management Office (DMO) a division of the HM Treasury.
19. The cash balance at 31st March 2003 was £143.1m, held in deposits with institutions set out in the table below. (£22.8m of the £143.1m was managed by Invesco). The return on cash closely tracks short term money market rates, which in turn closely follow base rates. In 2002/03 against average bases rates of c.4%, in-house return was 4.36% and Invesco's return was 4.50%. The interest earned for the year was £5.76m (£6.78m 2001/02).

Institution	Country	£m
UK DMO (HM Treasury)	United Kingdom	49.4
Bank of Scotland	United Kingdom	15.0
Lloyds TSB Bank	United Kingdom	10.4
Abbey National	United Kingdom	10.0
National Australia Bank	Australia	10.0
Barclays Bank	United Kingdom	17.5
Deutschebank	Germany	10.0
ABN AMRO	Netherlands	6.0
Credit Suisse	Switzerland	6.0
RBS/Natwest	United Kingdom	5.1
Landesbank Baden Weurttemberg	Germany	3.5
Bank of Ireland	Ireland	0.2
Total		£143.1m

Cash Management 2003/04 - Update

20. Returns in 2003/04 are expected to be somewhat lower as the UK economy adjusts to slower domestic and international growth. Some commentators see the recent base rate cut as temporary and predict rate rises later in the financial year as the economy improves; although the outlook is far from certain.

LEGAL IMPLICATIONS

21. The legal framework which governs the Council's financial management, borrowing and treasury management activities derives principally from the Local Government Act 1972 and the Local Government and Housing Act 1989.
22. Section 45 of the 1989 Act requires the Council to determine its overall borrowing limit, variable borrowing limit and short term borrowing limit in advance of the financial year to which those limits will apply. Such decisions must be taken by the Council itself and cannot be delegated to a committee, sub-committee or officer. This requirement has been complied with.

CONSULTATION

23. A copy of this report will be dispatched for Staff Side when the agenda for the meeting is dispatched.

BACKGROUND DOCUMENTS

Background Papers	Held at	Contact
Council Assembly: Treasury Management Strategy and Borrowing Limits 2002/03 25 th February 2002	Financial Management Services	Alan Layton, Head of Corporate & Strategic Finance (020 7525 4309)
Treasury Management Manual	Financial Management Services	Alan Layton, Head of Corporate & Strategic Finance (020 7525 4309)

APPENDIX A

Audit Trail

Lead Officer	Keith Brown , Chief Finance Officer	
Report Author	Alan Layton , Head of Corporate and Strategic Finance	
Version	Final	
Version Date	21/07/2003	
Key Decision	No	
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / EXECUTIVE MEMBER		
Officer Title	Comments Sought	Comments Included
Borough Solicitor & Secretary	Yes	Yes
Executive Member	Yes	No
Date Final Report Sent to Constitutional Support Services	21/07/2003	