

Item No: 8.2	Classification: Open	Date: 10 July 2013	Meeting Name: Council Assembly
Report title:		Treasury Management Performance - 2012/13 Annual Report and Prudential Indicators for Capital Finance and Treasury Management	
Wards or groups affected:		All	
From:		Strategic Director of Finance and Corporate Services	

RECOMMENDATION

1. That council assembly notes the 2012/13 outturn report on treasury management and prudential indicators.

BACKGROUND INFORMATION

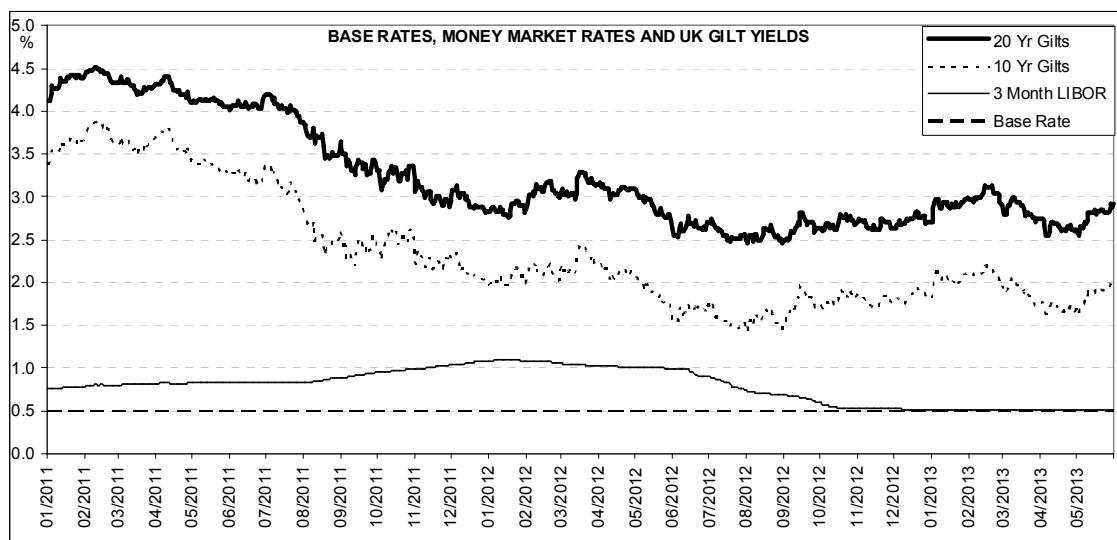
2. This item is one of an annual cycle of reports on the council's debt and investments. Other reports to council assembly on treasury include a strategy report at the start of each financial year and a half year update. The cabinet also receive quarterly updates and the audit and governance committee reviews treasury strategy annually.
3. Treasury activity is supported by a series of prudential indicators (estimates and limits on capital finance, debt and investments), which are agreed by council assembly each year and under financial delegation all executive, managerial and operational decisions are the responsibility of the strategic director of finance and corporate services. This area of finance falls under the Local Government Act 2003 and is supplemented by investment guidance issued by the government and codes of practice issued by the Chartered Institute of Public Finance and Accountancy (CIPFA).

KEY ISSUES FOR CONSIDERATION

Developments in Financial Markets

4. In 2012/13, financial markets remained sensitive to global economic developments, especially in the euro area, and the monetary policies of major central banks. Spanish and Italian government bond yields rose in the first four months of 2012/13, as declining expectations of growth raised uncertainty over the fiscal path and competitiveness of those countries. This led capital to flow into safer euro states (such as Germany, France and the Netherlands) as well as better rated countries (such as the US and UK) and lowered their sovereigns' bond yields. However news, in August 2012, that the European Central Bank (ECB) was prepared to purchase peripheral area government bonds reversed the climb in Spanish and Italian yields and lowered the attraction of safe haven states such as the UK where yields rose somewhat. The markets were also supported by a major plan by the Bank of Japan to purchase financial assets.
5. Central bank policies were also supportive to banks and led to lower bank funding costs. News of the one notch downgrade to UK's sovereign rating by Moody's and Fitch had no material impact. The Moody's change from Aaa to

Aa1 came in February 2013 and Fitch followed in April 2013 with a reduction from AAA to AA+. However since then, improvements in the outlook for the United States raised concerns that the Federal Reserve would taper off monetary easing sooner rather than later. This raised sovereign bond yields in the US and elsewhere, including in the UK. UK government bond yields (gilt yields) influence Public Works Loans Board (PWLB) lending rates to councils and bank funding costs affect returns on short term investments. The chart below shows recent gilt yields and short term bank funding cost (three month LIBOR in the chart).



Investment Management Activity and Position

6. Amid continued volatility in financial markets, the council maintained a cautious approach to its investments, prioritising security and liquidity as required under government guidance on local authority investments. Investment exposure to banks was diversified across large institutions in stronger sovereigns where the likelihood of support, in the event it were needed, was high and any exposure to investments above one year was in UK gilts or supranational bonds.

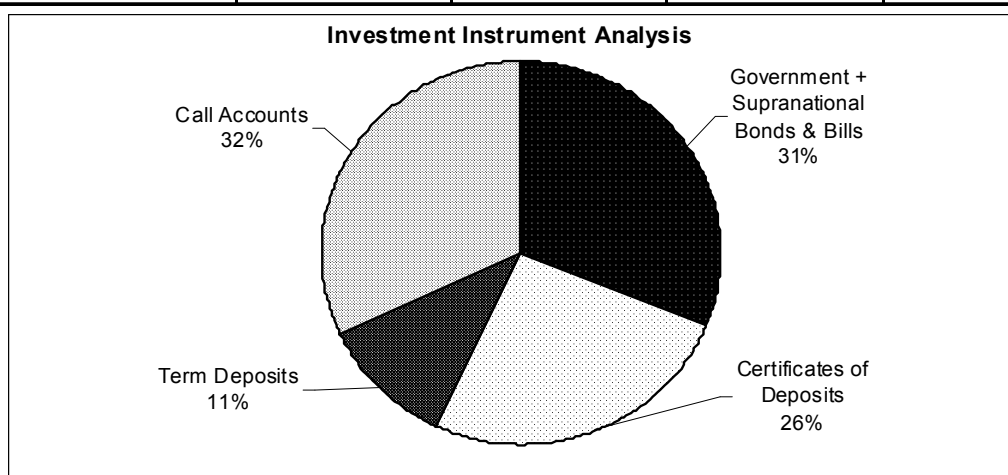
7. Over the course of 2012/13 the sums held in investments averaged £293m (£299m in 2011/12). The sums available for investment were affected by cash used in debt refinancing and the acquisition in December 2012 of the freehold interest in the council's headquarters at 160 Tooley Street. The investments are managed by an in-house operation and fund managers. Following a review of fund managers in May 2012, contracts with Aberdeen Asset Managers and AllianceBernstein were extended for a further three years. A new custodian, the Bank of New York Mellon, London Branch, (BNYM) (a US incorporated global financial institution and one of the largest custodians in the world) was appointed in July 2012 to replace HSBC who were previously providing the service. At close of 2012/13 investments stood at £176m (£187m at 31 March 2012). The distribution of these across counterparties, rating and maturity is set out in the tables and chart below. The average return for the year was 0.89% (1.03% in 2011/12), reflecting low money market and base rates.

EXPOSURE - MARCH 2013 COUNTERPARTY AND RATINGS										
COUNTERPARTY	FUND				Fitch Ratings					
	Aberdeen	Alliance Bernstein	In-House	£m	Long	Short	Sup- port	Sovereign	Sovereign Rating	
CREDIT INDUST ET COMRCIAL	3.5	-	-	3.5	A+	F1+	1	FRANCE	AAA	
SOCIETE GENERALE	-	1.0	-	1.0	A+	F1+	1	FRANCE	AAA	
BANQUE NATIONAL DE PARIS	3.5	1.0	-	4.5	A+	F1+	1	FRANCE	AAA	
DEUTSCHE BANK	3.5	1.0	-	4.5	A+	F1+	1	GERMANY	AAA	
LANDESBK BADEN WERT MBG	-	1.0	-	1.0	A+	F1+	1	GERMANY	AAA	
DZ BANK	3.5	-	-	3.5	A+	F1+	0	GERMANY	AAA	
ABN AMRO BK	3.5	1.0	-	4.5	A+	F1+	1	NETHERLANDS	AAA	
ING BK	3.4	1.0	-	4.4	A+	F1+	1	NETHERLANDS	AAA	
RABOBANK	-	0.5	-	0.5	AA	F1+	0	NETHERLANDS	AAA	
EUROPEAN INV BANK	7.0	6.6	-	13.6	AAA	F1+	0	SUPRANATIONAL	AAA	
INT BK RECONST DEVT	3.5	6.8	-	10.3	AAA	F1+	0	SUPRANATIONAL	AAA	
EUROPEAN BNK RECON DEV	3.4	-	-	3.4	AAA	F1+	1	SUPRANATIONAL	AAA	
SVENSKA	-	0.5	-	0.5	AA-	F1+	1	SWEDEN	AAA	
SKANDINAVISKA	-	1.0	-	1.0	A+	F1	1	SWEDEN	AAA	
UBS	3.5	-	-	3.5	A	F1	1	SWITZERLAND	AAA	
BARCLAYS BANK	5.0	-	-	5.0	A	F1	1	UK	AAA	
LLOYDS TSB/BK SCOTLAND	3.5	-	15.0	18.5	A	F1	1	UK	AAA	
NATIONWIDE BSOC	3.3	1.0	-	4.3	A+	F1	1	UK	AAA	
RBS/NATWEST	-	-	61.7	61.7	A	F1	0	UK	AAA	
UK TREASURY	-	26.8	-	26.8	AAA	F1+	1	UK	AAA	
BNY MELLON	0.1	1.1	-	1.2	AA-	F1+		US	AAA	
Total Gross £m (#)	50.2	50.3	76.7	177.2						

(#) Includes sums held on behalf of trust fund accounts. The council's own investments, excluding trust funds, are £176m.

NB. Fitch rating in this table is as at March 2013. As detailed in paragraph 5, the rating for UK Treasury was revised in April 2013.

Investment Rating and Maturity				
Rating	AAA	AA+ to AA-	A+ to A	Total
Period Remaining				
2-5 years	7%			7%
1-2 years	9%			9%
Less than 1 year	14%	1%	69%	84%
	30%	1%	69%	100%

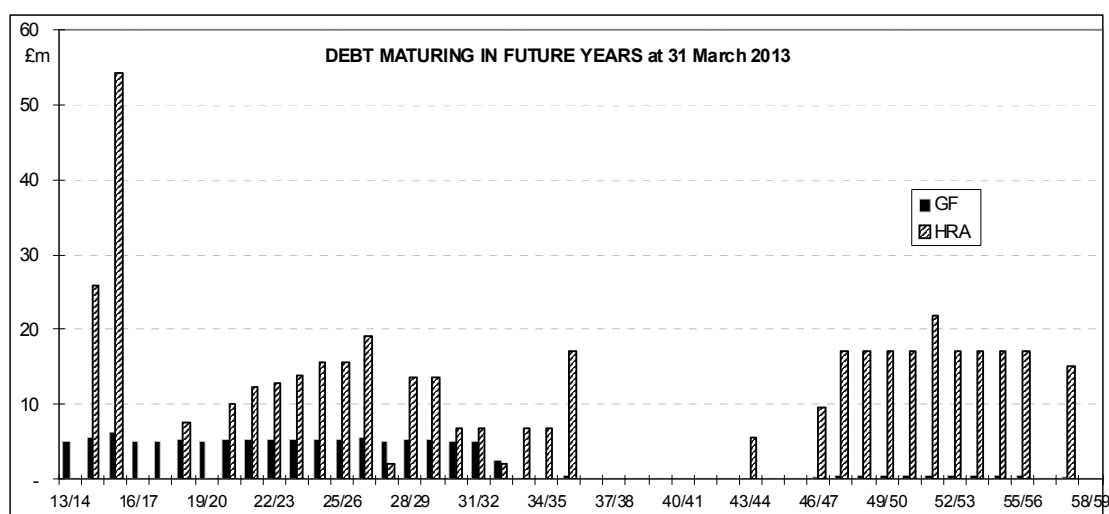


Debt Management Activity and Position

- The opening debt balance as at 1 April 2012 was £462m. During the financial year 2012/13 £100m was borrowed at 3.20%, repayable in equal instalments over 20 years. The first instalment of £2.5m fell due in 2012/13 and has been paid, which brings the total debt outstanding at 31 March 2013 to £560m.
- From April 2012 the debt has been disaggregated between the Housing Revenue Account (HRA) and the General Fund (GF) and each fund can now

manage its debt in a way that best suits its need. At 1 April 2012, the HRA debt stood at £451m and the GF debt at £12m. The GF element rose during 2012/13 when £100m in new loans were taken to replace the repayment made in March 2012. After repaying £2.5m of the new loan, the GF debt stands at £109m at 31 March 2013. The HRA debt has remained unchanged throughout 2012/13 and unlike the GF, there is no statutory requirement to set-aside sums from revenue to pay it off.

10. All the debt is from the PWLB at fixed rates and the maturity profile of the £560m outstanding at 31 March 2013 is set out in the chart below. The average rate of interest in 2012/13 on HRA debt is 6.55% and for GF is 3.57%. The GF rate reflects the low coupon loans taken in April 2012. The HRA will see its average rate fall once high rate maturing loans are replaced with lower rate ones – it has some £80m maturing between 2014/15 and 2015/16.



Prudential Indicators Outturn

11. Prudential indicators consist of a series of estimates and limits to give a general picture of the affordability, prudence and sustainability of capital finance and treasury management. The indicators are drawn from the Prudential Code for Capital Finance in Local Authorities and the Treasury Management Code of Practice and Guidance.
12. The outturn for each indicator based on 2012/13 draft accounts is set out in Appendix A and includes the authorised debt limit, which is a self imposed cap on borrowing and other long term liabilities (like leases and PFI schemes) outstanding on any one day. The limit for 2012/13 was £885m and included operational flexibility for temporary borrowing and prudent refinancing within a risk controlled framework. The maximum debt and long term liabilities outstanding at any one time during 2012/13 was £562m and £107m respectively and together remained below the authorised limit.

Capital Allowances

13. Following an announcement in January 2013, the Department of Communities and Local Government went ahead with proposal to abolish capital allowances from April 2013. Capital allowances were a mechanism that gave councils the power to retain non-right-to-buy housing receipts (such as receipts from sale of vacant land and garages) for use in affordable housing and regeneration. Each year council assembly made a determination in relation to such allowances to ensure that non-right-to-buy housing receipts were retained, rather than passed

to the government in pooling. However, following concerns raised by local authorities that abolition of capital allowances would mean loss of resources for affordable housing and regeneration, the Department introduced a new regulation to restore the power to use non-right-to-buy housing receipts for affordable housing and regeneration. The new power means that these receipts can be retained without council assembly having to make a determination on capital allowances each year.

SUPPLEMENTAL ADVICE FROM OTHER OFFICERS

Director of Legal Services

14. The constitution determines that agreeing the treasury management strategy is a function of the council assembly and that review and scrutiny of strategies and policies is the responsibility of the audit and governance committee.
15. Financial standing orders require the strategic director of finance and corporate services to set out the treasury management strategy for consideration and decision by council assembly, and report on activity on a quarterly basis to cabinet and at mid and year-end to council assembly. Furthermore all executive and operational decisions are delegated to the strategic director of finance and corporate services.
16. The Local Government Act 2003 and supporting regulations require local authorities to determine annual borrowing limits and have regard to the Prudential Code for Capital Finance, and the Treasury Management in the Public Services Code of Practice and Guidance, published by the Chartered Institute of Public Finance and Accountancy, when considering borrowing and investment strategies, determining or changing borrowing limits or prudential indicators.
17. Section 15(1) of the 2003 Act requires a local authority “to have regard (a) to such guidance as the Secretary of State may issue”. This guidance is found in the Department of Communities and Local Government Guidance on Local Authority Investments updated March 2010 and there is statutory guidance on the Minimum Revenue Provision (MRP) produced under amendments made to section 21(1A) of the 2003 Act by section 238(2) of the Local Government and the Public Involvement in Health Act 2007.
18. Section 12 of the 2003 Act grants local authorities the powers to invest for any purpose relevant to its functions or for the purposes of the prudent management of its financial affairs.

BACKGROUND DOCUMENTS

Background Papers	Held at	Contact
None		

APPENDICES

No.	Title
Appendix A	Prudential Indicators – 2012/13 Outturn

AUDIT TRAIL

Lead Officer	Duncan Whitfield, Strategic Director of Finance and Corporate Services	
Report Author	Jennifer Seeley, Deputy Finance Director	
Version	Final	
Version Date	26 June 2013	
Key Decision	Yes	
CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / CABINET MEMBER		
Officer Title	Comments Sought	Comments Included
Director of Legal Services	Yes	Yes
Strategic Director of Finance and Corporate Services	N/A	N/A
Cabinet Member	Yes	Yes
Final Report Sent to Constitutional Team		27 June 2013