

HAMBLETON DISTRICT COUNCIL

Report To: Cabinet
11 September 2012

Subject: ANNUAL TREASURY MANAGEMENT REPORT 2011/12

All Wards
Audit, Governance and Standards Committee
Portfolio Holder for Resources: Councillor R Kirk

1.0 PURPOSE AND BACKGROUND:

- 1.1 The purpose of this report is to present a summary of the treasury management activities for the last financial year (2011/12) in line with the Treasury Management Code of Practice.
- 1.2 The Annual Treasury Management Report for 2011/12 is attached as Annex A. It is presented as part of the Code's requirement to present regular reports to Members on Treasury Management. The report sets out the Treasury Management position for 2011/12 and how the Council has performed in this area.

2.0 DECISION SOUGHT:

- 2.1 Members are asked to consider the contents of the Annual Treasury Management Report for 2011/12.

3.0 RISK ANALYSIS:

- 3.1 There are no major risks associated with the recommendations of this report. The Council's Constitution (under the Treasury Management section of the Financial Procedure Rules) requires that Cabinet receive an annual report on treasury management activities. If a report was not forthcoming to Cabinet, it would clearly breach the Constitution, and Members would not be kept informed of activities in this important aspect of the Council's finances. In addition, I would expect the Council's external auditors, Deloitte, to comment on the omission as part of their annual audit and inspection work.

4.0 FINANCIAL IMPLICATIONS AND EFFICIENCIES:

- 4.1 There are no financial implications in approving this report although Members may wish to note that income from investments exceeded the budget by £30,419 (see paragraph 12 of Annex A).

5.0 RECOMMENDATION:

- 5.1 It is recommended to Council that, subject to any comments from the Audit, Governance and Standards Committee, the Annual Treasury Management Report for 2011/12 is approved.

CLAIRE BLACKBURN

Background papers: None
Author ref: CB
Contact: Claire Blackburn
Finance Manager
Direct Line No: 827117

ANNUAL TREASURY MANAGEMENT REPORT FOR 2011/12

1.0 PURPOSE:

- 1.1 This Council is required through regulations issued under the Local Government Act 2003 to produce an annual treasury report reviewing treasury management activities and the actual prudential and treasury indicators for 2011/12. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).
- 1.2 During 2011/12 the minimum reporting requirements were that the full Council should receive the following reports:
- an annual treasury strategy in advance of the year (Cabinet 22/03/11)
 - a mid year (minimum) treasury update report (Cabinet 29/11/11)
 - an annual report following the year describing the activity compared to the strategy (this report)
- 1.3 Changes in the regulatory environment place a much greater onus on members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by members.
- 1.4 This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to all of the above treasury management reports by the Audit and Governance Committee before they were reported to the full Council.

2.0 EXECUTIVE SUMMARY:

- 2.1 During 2011/12, the Council complied with its legislative and regulatory requirements. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

Prudential and Treasury Indicators	2010/11 Actual £000	2011/12 Original £000	2011/12 Actual £000
Actual Capital Expenditure	1,562	2,185	983
Total Capital Financing Requirement:			
• Non-HRA	-	-	-
• Housing Revenue Account (HRA)	-	-	-
• Total	-	-	-
Net Borrowing	-	-	-
External Debt	-	-	-
Investments:			
• Longer than 1 year	-	-	-
• Under 1 year	18,600	18,600	19,000
• Total	18,600	18,600	19,000

2.2 Other prudential and treasury indicators are to be found in the main body of this report. The S151 Officer and the Finance Manager also confirms that no external borrowing for capital purposes was undertaken and the statutory borrowing limit (the authorised limit), was not breached.

2.3 The financial year 2011/12 continued the challenging environment of previous years; low investment returns and continuing counterparty risk continued.

3.0 **INTRODUCTION AND BACKGROUND:**

3.1 This report summarises:

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- Reporting of the required prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity;
- Detailed investment activity;

4.0 **THE COUNCIL'S CAPITAL EXPENDITURE AND FINANCING 2011/12:**

4.1 The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

4.2 The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

	2010/11 Actual £000	2011/12 Original £000	2011/12 Actual £000
Non-HRA capital expenditure	1,562	2,185	983
HRA capital expenditure	-		
Total capital expenditure	1,562	2,185	983
Resourced by:			
• Capital Receipts	749	1,405	203
• Capital Grants	797	780	781
• Capital Reserves	14	-	-
• Revenue	2	-	-
Unfinanced capital expenditure	-	-	-

5.0 **THE COUNCIL'S OVERALL BORROWING NEED:**

5.1 A Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of a Council's debt position. The CFR results from the capital activity of a Council and what resources have been used to pay for the capital spend. The CFR represents the 2011/12 unfinanced capital expenditure

and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources (see above table).

- 5.2 As a debt free authority the Council does not have a CFR.
- 5.3 **The authorised limit** - the authorised limit is the “affordable borrowing limit” required by s3 of the Local Government Act 2003. The Council does not have the power to borrow above this level. The table below demonstrates that during 2011/12 the Council has maintained gross borrowing within its authorised limit.
- 5.4 **The operational boundary** – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached.
- 5.5 **Actual financing costs as a proportion of net revenue stream** - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2011/12
Authorised limit	£5.0 m
Maximum gross borrowing position	£0.0 m
Operational boundary	£4.0 m
Average gross borrowing position	£0.0 m
Financing costs as a proportion of net revenue stream	0.0 %

6.0 TREASURY POSITION AS AT 31 MARCH 2012:

- 6.1 The Council's debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through Member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices. At the beginning and the end of 2011/12 the Council's treasury position was as follows:

	1 April 2011	Rate %	31 March 2012	Rate %
Fixed Rate Funding:				
- PWLB	-	0.0%	-	0.0%
- Market	-		-	
	-		-	
Variable Rate Funding:				
- PWLB	-		-	
- Market	-		-	
	-		-	
	-		-	
Total Debt	-	0.0%	-	0.0%
CFR	-		-	
Over/(Under) Borrowing	-		-	
Investments				
- In-house	18,600		19,000	
- Fund Managers	-		-	
Total Investments	18,600		19,000	

6.2 The maturity structure of the debt portfolio was as follows:

	31 March 2011 Actual	2011/12 Original Limits	31 March 2012 Actual
Under 12 months	£0.00 m	£0.00 m	£0.00 m
12 months and within 24 months	£0.00 m	£0.00 m	£0.00 m
24 months and within 5 years	£0.00 m	£0.00 m	£0.00 m
5 years and within 10 years	£0.00 m	£0.00 m	£0.00 m
10 years and above	£0.00 m	£0.00 m	£0.00 m

6.3 The maturity structure of the investment portfolio was as follows:

	2010/11 Actual £000's	2011/12 Original £000's	2011/12 Actual £000's
Investments:			
- Longer than 1 year	-	-	-
- Under 1 year	18,600	18,600	19,000
Total Investments	18,600	18,600	19,000

6.4 The exposure to fixed and variable rate investments was as follows:

	31 March 2011 Actual	2011/12 Original Limits	31 March 2012 Actual
Fixed Rate	18,600	18,600	19,000
Variable Rate	-	-	-

7.0 THE STRATEGY FOR 2011/12:

7.1 The strategy for 2011/12 did not anticipate any need to borrow during the year although the option was kept open should there be a need to borrow identified.

7.2 **Change in strategy during the year** – the strategy adopted in the original Treasury Management Strategy Report for 2011/12 approved by the Council on 12 April 2011 was not changed throughout the financial year 2011/12.

8.0 THE ECONOMY AND INTEREST RATES:

8.1 The financial year 2011/12 continued the challenging investment environment of previous years, namely low investment returns and continuing heightened levels of counterparty risk. The original expectation for 2011/12 was that Bank Rate would start gently rising from quarter 4 2011. However, economic growth in the UK was disappointing during the year due to the UK austerity programme, weak consumer confidence and spending, a lack of rebalancing of the UK economy to exporting and weak growth in our biggest export market - the European Union (EU). The UK coalition Government maintained its tight fiscal policy stance against a background of warnings from two credit rating agencies that the UK could lose its AAA credit rating. Key to retaining this rating will be a return to strong economic growth in order to reduce the national debt burden to a sustainable level, within the austerity plan timeframe. The USA and France lost their AAA credit ratings from one rating agency during the year. Weak UK growth resulted in the Monetary Policy Committee increasing quantitative easing by £75bn in October and another £50bn in February. Bank Rate therefore ended the year unchanged at 0.5% while CPI inflation peaked in September at 5.2%, finishing at 3.5% in March, with further falls expected to below 2% over the next

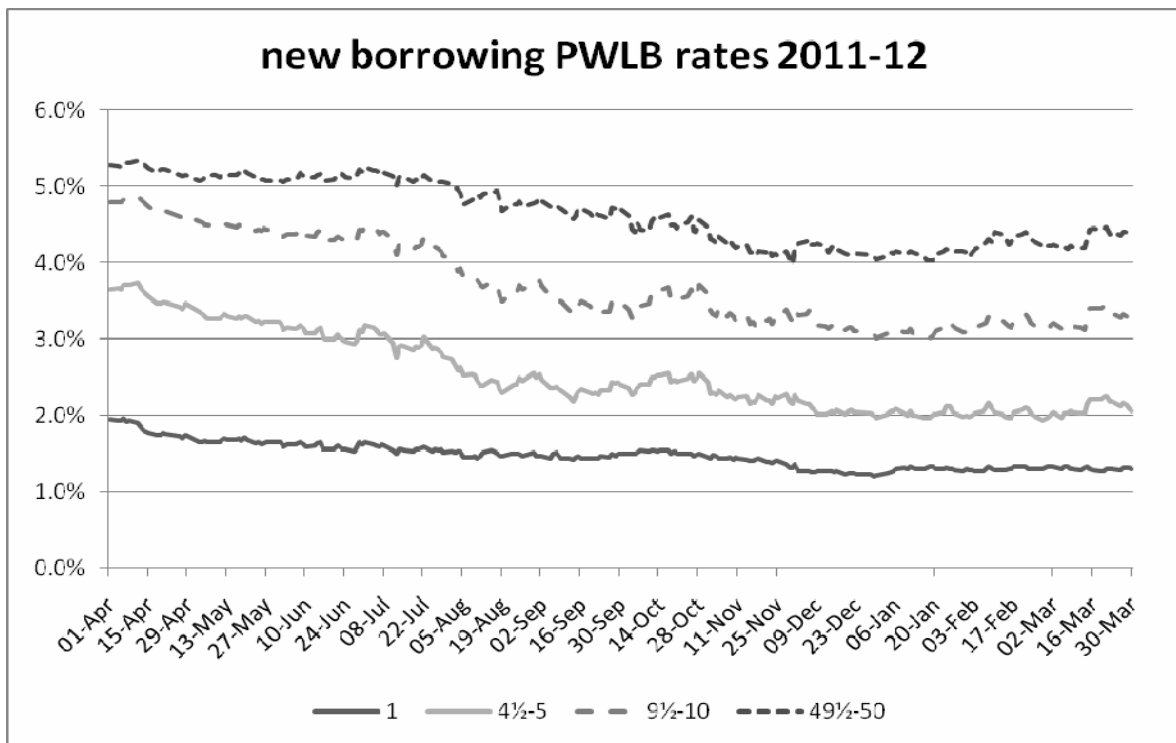
two years. The EU sovereign debt crisis grew in intensity during the year until February when a second bailout package was eventually agreed for Greece.

Gilt yields fell for much of the year, until February, as concerns continued building over the EU debt crisis. This resulted in safe haven flows into UK gilts which, together with the two UK packages of quantitative easing during the year, combined to depress PWLB rates to historically low levels.

Investment rates. Risk premiums were also a constant factor in raising money market deposit rates for periods longer than 1 month. Widespread and multiple downgrades of the ratings of many banks and sovereigns, continued Eurozone concerns, and the significant funding issues still faced by many financial institutions, meant that investors remained cautious of longer-term commitment.

9.0 **BORROWING RATES IN 2011/12:**

9.1 **PWLB borrowing rates** - the graph below shows how PWLB rates fell to historically very low levels during the year.



10.0 **THE BORROWING OUTTURN FOR 2011/12:**

10.1 **Treasury Borrowing** – the Council undertook no external borrowing for cash flow purposes during 2011/12.

10.2 **Borrowing** – the Council undertook no external borrowing for financing purposes during 2011/12. The capital programme was financed by a mixture of external grants, capital receipts, reserve funding and revenue contributions.

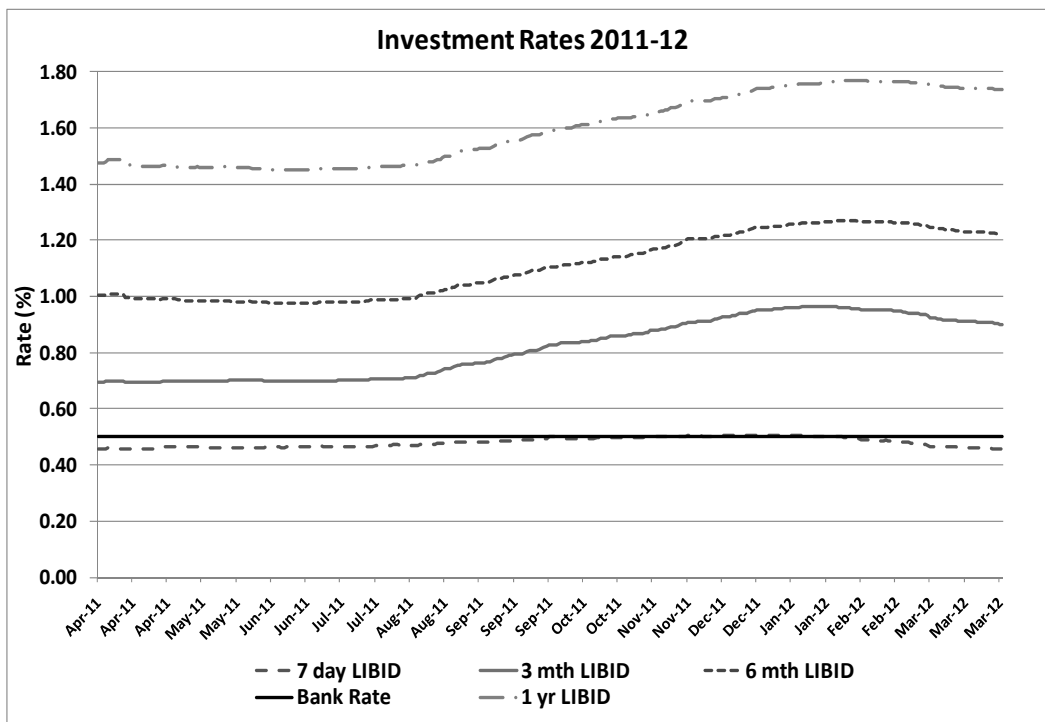
10.3 **Rescheduling** – the Council undertook no rescheduling of debt during 2011/12.

10.4 **Repayment** – the Council has no external loans and therefore no repayments were necessary.

11.0 **INVESTMENT RATES IN 2011/12:**

11.1 The tight monetary conditions following the 2008 financial crisis continued through 2011/12 with little material movement in the shorter term deposit rates. However, one month and longer rates rose significantly in the second half of the year as the Eurozone crisis grew. Bank Rate remained at its historic low of 0.5% throughout the year while market expectations of the start of monetary tightening were gradually pushed further and further back during the year to the second half of 2013 at the earliest.

Overlaying the relatively poor investment returns were the continued counterparty concerns generated by the Eurozone sovereign debt crisis.



12.0 **INVESTMENT OUTTURN FOR 2011/12:**

12.1 **Investment Policy** – the Council's investment policy is governed by CLG guidance, which was been implemented in the annual investment strategy approved by the Council on 12 April 2011. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

12.2 The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

12.3 **Investments held by the Council** - the Council maintained an average balance of £26,113,000 of core cash investments. These internally managed funds earned an average rate of return of 1.56%, yielding £409,077 of interest. The comparable performance indicator is the average 7-day LIBID rate, which was 0.480%. This compares with a budget assumption of £26,000,000 investment balances earning an average rate of 1.5% and a budget of £395,000 for interest.

12.4 In addition, the Council manages cash flow money. During the year the Council maintained an average balance of £4,292,000 of cash flow investments. These internally managed funds earned an average rate of return of 0.85%, yielding £36,342 of interest. The comparable performance indicator is the average 7-day LIBID rate, which was 0.480%. This compares with a budget assumption of £2,857,000 investment balances earning an average rate of 0.70% and a budget of £20,000 for interest.

13.0 ICELANDIC BANK DEFAULTS AND OTHER ISSUES:

13.1 To complete the review of fund management activities for 2011/12 it is worth reminding ourselves of two connected issues.

13.2 Firstly, the Council did not hold any investments in the Icelandic banks which collapsed in October 2008, and no institutions in which investments were made during 2011/12 had any difficulty in repaying investments and interest in full during the year.

13.3 Secondly, the collapse of the Icelandic banks was the beginning of an unparalleled banking crisis that spread across the world and affected the banking sector and other market institutions as well as the world economies in general. It resulted in uncertainties in the market place that are still being felt today making budgetary and performance targets in this area difficult to predict with any level of certainty.

PRUDENTIAL INDICATORS – OUTTURN 2011/12

PRUDENTIAL INDICATORS	2010/11	2011/12	2011/12
Extract from budget and rent setting report	actual	original	Actual
	£'000	£'000	£'000
Capital Expenditure			
Non - HRA	£1,562	£2,185	£983
HRA (applies only to housing authorities)	-	-	-
TOTAL	£1,562	£2,185	£983
Ratio of financing costs to net revenue stream			
Non - HRA	N/A	N/A	N/A
HRA (applies only to housing authorities)	-	-	-
Net borrowing requirement			
brought forward 1 April	Nil	Nil	Nil
carried forward 31 March	Nil	Nil	Nil
in year borrowing requirement	Nil	Nil	Nil
Capital Financing Requirement as at 31 March			
Non – HRA	Nil	Nil	Nil
HRA (applies only to housing authorities)	-	-	-
TOTAL	Nil	Nil	Nil
Annual change in Cap. Financing Requirement			
Non – HRA	Nil	Nil	Nil
HRA (applies only to housing authorities)	-	-	-
TOTAL	Nil	Nil	Nil
Incremental impact of capital investment decisions	£ p	£ p	£ p
Increase in council tax (band D) per annum	£4.21	5.43	2.64
Increase in average housing rent per week (housing authorities only)	-	-	-

TREASURY MANAGEMENT INDICATORS	2010/11	2011/12	2011/12
	actual	original	actual
	£'000	£'000	£'000
Authorised Limit for external debt -			
borrowing	£5,000	£5,000	£5,000
other long term liabilities	-	-	-
TOTAL	£5,000	£5,000	£5,000
Operational Boundary for external debt -			
borrowing	£4,000	£4,000	£4,000
other long term liabilities	-	-	-
TOTAL	£4,000	£4,000	£4,000
Actual External Debt	Nil	Nil	Nil
Upper limit for fixed interest rate exposure expressed as:- Net principal re fixed rate borrowing / investments:-	£5,000	£5,000	£5,000
Upper limit for variable rate exposure expressed as:- Net principal re variable rate borrowing / investments	Nil	Nil	Nil
Upper limit for total principal sums invested for over 364 days (per maturity date)	£12,500	£12,500	£12,500

Maturity structure of fixed rate borrowing during 2011/12	upper limit	lower limit
under 12 months	100%	100%
12 months and within 24 months	0%	0%
24 months and within 5 years	0%	0%
5 years and within 10 years	0%	0%
10 years and above	0%	0%