REPORT OF THE SERVICE DIRECTOR – FINANCE AND PROCUREMENT

TREASURY MANAGEMENT OUTTURN REPORT 2012-13

1. Purpose

To provide a review of the Council's treasury management activities for the year to 31 March 2013.

Information and Advice

2. Background

2.1 Treasury management is defined as "the management of the council's investments and cashflows; its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

2.2 The Council's Treasury Management Strategy is approved annually by Full Council and there will also be a mid year report which will go to Full Council. Responsibility for the implementation, scrutiny and monitoring of treasury management policies and practices is delegated to the *Treasury Management Group*, comprising the Service Director (Finance & Procurement), the Group Manager (Financial Strategy & Compliance), the Senior Accountant (Pensions & Treasury Management) and the Senior Finance Business Partner (Capital & External Funding).

2.3 In 2012/13, borrowing and investment activities have been in accordance with the approved limits as set out in the Council's Treasury Management Policy and Strategy. The main points from this report are:

- All treasury management activities were effected by authorised officers within the limits agreed by the Council
- All investments were made to counterparties on the Council's approved lending list
- £40m of long-term borrowing was raised in 2012/13
- The Council earned 1.19% on its cash investments, outperforming the average 7 day London Interbank BID rate of 0.39%.
- Reports have been submitted to Council and the Finance and Property committee as required.

3. Outturn Treasury Position

3.1 The Council's treasury management strategy and associated policies and practices for 2012/13 were approved on 23 February 2012 by Full Council. The Service Director (Finance & Procurement) complied with the strategy throughout the financial year 2012/13. The Council's treasury portfolio position at 31 March 2013 is shown in Table 1 below.

Table 1. Treasury Position at 31 March 2013		**£m**	**£m**	**Average Interest Rate**
EXTERNAL BORROWING				
Fixed Rate	PWLB	209.9		6.34%
	Market Loan	100.0		3.85%
	Other	10.0	319.9	0.78%
Variable Rate	PWLB	0.0		
	Market Loan	0.0	0.0	
Total			**319.9**	5.44%
Other Long-Term Liabilities			**134.0**	
Total Gross Debt			**453.9**	
Less: Investments			41.6	1.19%
Total Net Debt			**412.3**	

Note 1: PWLB = Public Works Loans Board
Note 2: Market Loans = Lenders' Option, Borrowers' Option (LOBO) loans

4. Economic Background

4.1 The UK's economic performance over the past year is summarized in Table 2 below showing the quarterly percentage change for gross domestic product, the annualized change to the consumer price index each quarter together with the percentage unemployed each quarter. This shows the economy fell back into recession in 2012 following two consecutive quarters of negative growth but avoided a 'triple-dip' in the first quarter of 2013.

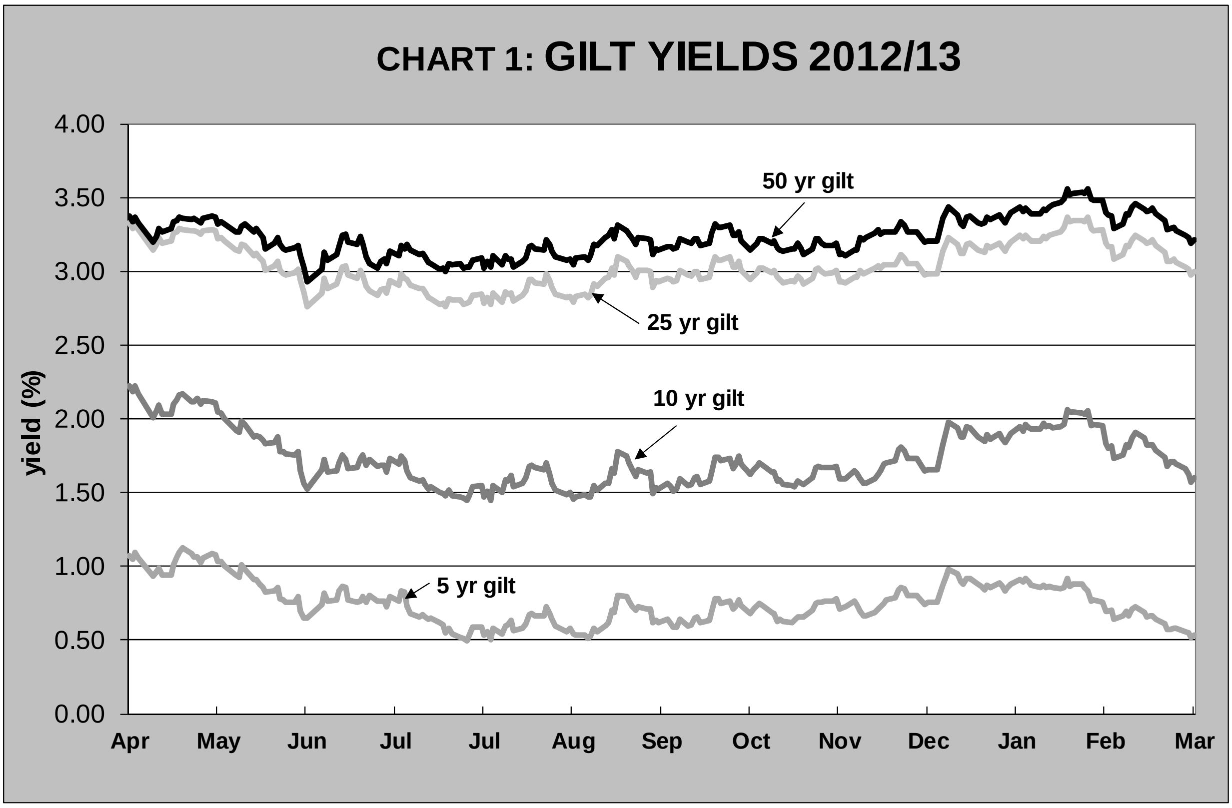
Table 2 Economic Indicators	**2012 Q1**	**2012 Q2**	**2012 Q3**	**2012 Q4**	**2013 Q1**
Consumer Prices Index	3.5	2.4	2.2	2.7	2.8
Gross Domestic Product	-0.1	-0.4	0.9	-0.3	0.3
Unemployment	8.3	8.0	7.8	7.8	7.8

4.2 The consumer price index reduced over the year to 2.8%, having peaked in the first quarter of 2012 at 3.5%. This fall is attributed mainly to external shocks to the price level, such as higher energy prices, and increases in administered and regulated prices last year that are working through the index. The latest inflation report from the Bank of England (BoE) expects inflation to be above the 2% target for the next 2 years before falling back due to domestic cost pressures being contained by rising productivity.

4.3 The lack of sustained growth in the UK economy has meant that the BoE has maintained base rates at 0.5% throughout the year with no immediate prospect of an increase. With inflation expected to be on target over the medium term additional quantitative easing of £50bn was undertaken in July 2012 to bring the total to £375bn.

4.4 Gilt yields drifted lower during the first half of the year with low points attained during the summer before rising through the autumn and then falling again by the end of March. This is shown in Chart 1. The 5 and 10 year gilts ended the year just above the lows reached in the summer, having risen more than 50 basis points by the end of December. These movements reflect a number of factors:

- Investor sentiment over prospects for global growth
- demand for gilts boosted by the BoE's quantitative easing programme
- loss of the UK's 'safe haven' status as the Eurozone crisis eased
- lower prospects for UK economic growth.



5. Treasury Management Activities 2012/13

5.1 The Council manages its investments in-house and invests with institutions on the Council's approved lending list, aiming to achieve the optimum return on investments commensurate with the proper levels of security and liquidity. The Council's temporary borrowing and lending activity over the year is set out in Table 3 below.

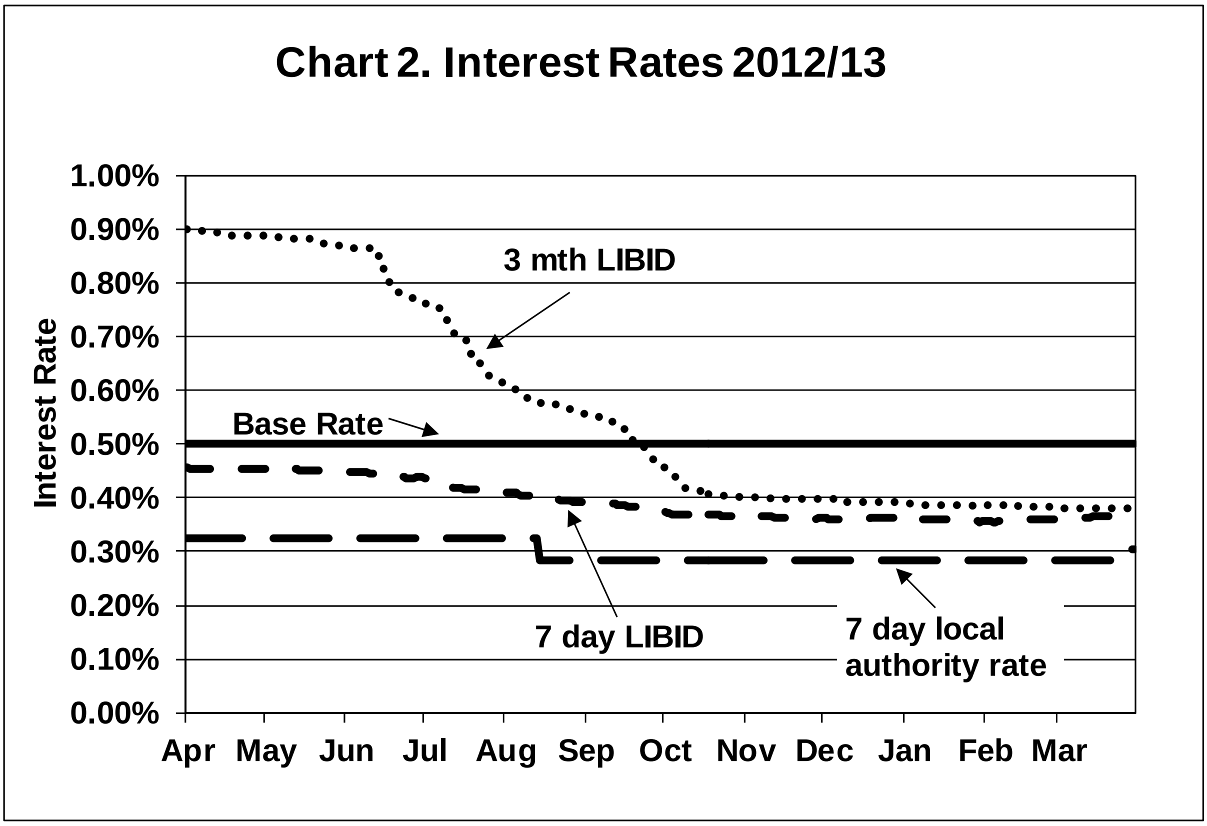
Table 3 Temporary Borrowing and Lending	**Borrowing £m**	**Lending £m**	**Net Position £m**
Outstanding 1 April 2012	0.0	(38.5)	(38.5)
Raised/ (lent) during period	177.8	(796.2)	(618.4)
Repayments during period	(177.8)	795.1	617.3
Outstanding 31 March 2013	0.0	(39.6)	(39.6)

5.2 Over the 12 months to 31 March 2013, the Council's cash flows were maintained through borrowing and lending activities on the wholesale money market and the net position at 31 March 2013 shows outstanding temporary lending of £39.6m. In addition, there was a further £2m invested for a period of 5 years as part of the Council's commitment to the Local Authority Mortgage Scheme. The average level of funds available for investment purposes over the year was £51.2m. This was mainly dependent on the timing of precept payments, receipt of grants, progress on the capital programme and net movement on creditors and debtors.

5.3 The Council's investment returns have significantly outperformed the benchmark, the 7-day London Interbank BID rate (LIBID) for the year which averaged 0.39% against actual returns of 1.19%, an outperformance of 0.80%. This equates to additional interest of over £400,000 for the year. Table 4 shows the returns achieved by type of investment. The use of fixed term investments of up to 364 days has allowed a higher return to be achieved and the use of call accounts has allowed the Council to optimize liquidity versus returns.

Table 4 Returns on Investments	**Average Balance £m**	**Interest Earned £k**	**Average Return %**
Fixed Term Investments (under 364 days)	30.0	457.9	1.53%
Fixed Term Investments (over 364 days)	0.2	4.8	2.24%
Bank Call Accounts	10.3	80.1	0.78%
Money Market Funds	10.7	65.9	0.62%
Total	**51.2**	**608.7**	**1.19%**

5.4 Investment rates available in the market are at a historical low point. Chart 2 shows how key benchmarks have moved over the year. Base rate remains at 0.5% but the 7 day and 3 month LIBID have fallen over the year, with the 3 month rate more than halving. This reflects the Bank of England's Funding for lending scheme introduced in July 2012 that provides cheaper loans to banks and as a consequence demand for funds from the money markets has fallen.

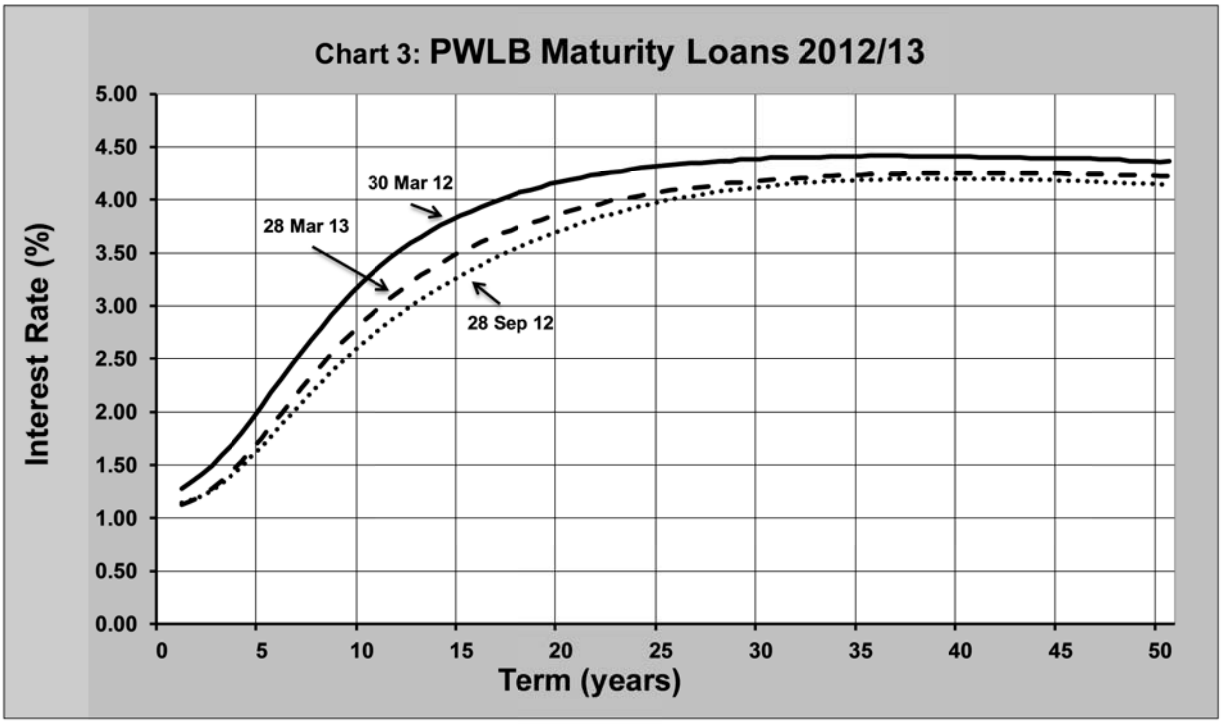


5.5 The Council has maintained average cash balances at around £50m in order to minimize long-term borrowing yet maintain sufficient liquidity to meet payments as they fall due. During the year temporary borrowing was required for a period of 35 days in total at an average rate of interest of 0.55%.

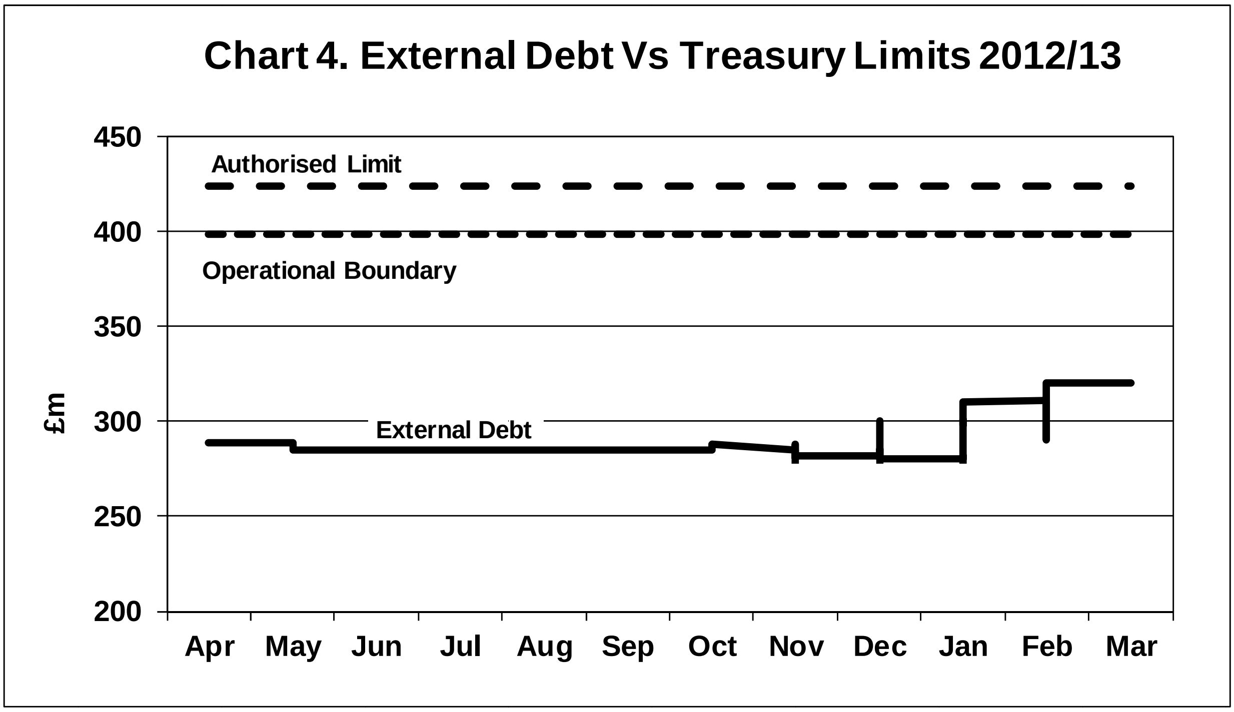
5.6 During the year as the crisis in the Eurozone developed the Treasury Management Group decided as a prudent measure to temporarily suspend Santander UK following concerns over its Spanish parent. In addition Dankse Bank was removed from the approved lending list due to a ratings downgrade.

6. Long Term Borrowing

6.1 The Council's Treasury Management Strategy for 2012/13 presented to Council in February 2012 outlined the Council's long term borrowing strategy for the year. The borrowing rates available from the PWLB reflect gilt yields which have fallen over the year as described in para. 4.4 above. Longer term borrowing rates were budgeted for at a 4.15% average borrowing rate but the graph below shows that interest rates have fallen with the low point being reached for most durations in July with the rates at the end of March 2013 around 20 basis points higher. In November the PWLB offered a reduction of 20 basis points for local authorities submitting additional financial data on their borrowing plans. The Council successfully applied for this 'certainty rate'.



6.2 Long term borrowing stood at £319.9m on the 31 March 2013 which is within the authorized limit agreed by the Council. Chart 4 below shows that the level of external debt throughout the year was below the key treasury indicators of the authorized limit and the operational boundary, demonstrating that borrowing was within plan during the year. Further details on these treasury prudential indicators are provided in Appendix F.



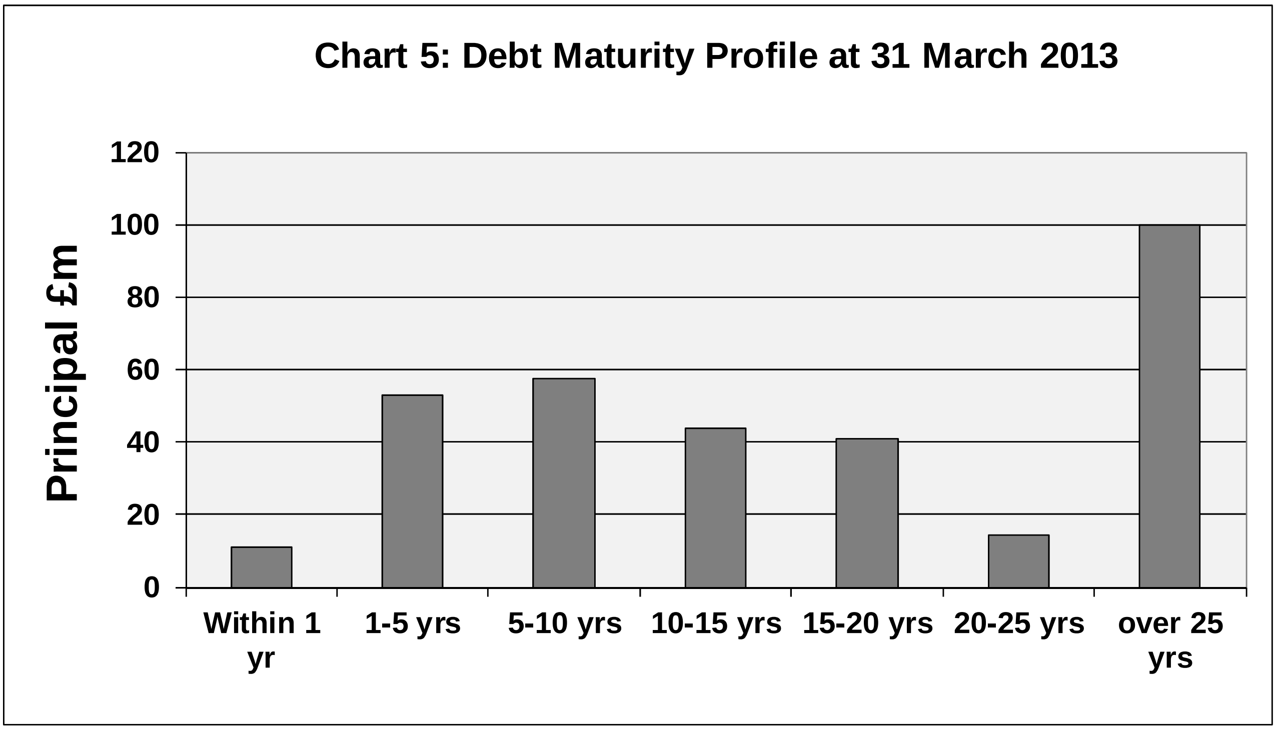
6.3 Net new borrowing of £31.1m in 2012/13 compares with an estimate of £100m in the approved strategy as a consequence of higher than anticipated cash balances and slippage on the capital programme. New borrowing totalling £30m was raised in February 2013 in the form of maturity loans from the PWLB for periods between 6 and 18 years at an average rate of 3.28%. A further £10m of loans were raised from the money markets at an average rate of 0.78% for periods up to 2 years.

6.4 The loan portfolio includes 10 LOBOs of £10m each. Two of these had call options in 2012/13 (whereby the lender can increase the interest rate payable) but these were not exercised. The rates on these loans ranged from 3.25% to 4.17% which compare favorably with the 50 year PWLB standard rate of 4.22% at the end of March 2013.

Table 5 Movements in Long-term Borrowing 2012-13

Lender	B/fwd 31/03/12 £m	Advances 2012/13 £m	Repayments at maturity 2012/13 £m	Premature Repayments 2012/13 £m	C/fwd 31/03/13 £m
PWLB	188.8	30.0	8.9	0.0	209.9
LOBO	100.0	0.0	0.0	0.0	100.0
Other	0.0	10.0	0.0	0.0	10.0
Total	288.8	40.0	8.9	0.0	319.9

6.5 The chart below shows that the debt maturity profile is well spread over the next 20 years with a maximum duration of 23 years for PWLB debt. The £100m shown in the over 25 year category comprises of LOBOs, the earliest redemption date of which is 2055. The average rate on external debt was 5.44% compared to 5.74% in the previous year.



6.6 The Council has the option of rescheduling its existing long-term debt should market conditions indicate opportunities for savings. This is achieved by redeeming fixed rate debt and raising new debt at a lower rate of interest. This opportunity is provided primarily for PWLB debt and may give rise to premiums or discounts depending on the rate differentials. No opportunities for debt rescheduling arose over the reporting period.

7. Prudential Indicators for Treasury Management

7.1 Table 6 below shows how the treasury management indicators compare with the outturn position. The objective of these indicators is to manage treasury management risks effectively. No indicators were breached during the year.

Table 6 **TREASURY MANAGEMENT INDICATORS 2012/13**	**Approved limits**	**Outturn**
Net Debt	£470m	£412m
Upper limit for Rate Exposure		
Fixed Rate	100%	100%
Variable Rate	75%	0%
Upper limit for principal sums invested for over 364 days	Higher of £20m and 15%	£2m

Maturity structure of fixed rate borrowing	**Approved Lower limit**	**Approved Upper limit**	**Outturn**
Under 12 months	0%	25%	3%
12 months and within 24 months	0%	25%	7%
24 months and within 5 years	0%	75%	10%
5 years and within 10 years	0%	100%	18%
10 years and above	0%	100%	62%
Adoption of CIPFA's Treasury Management in the Public Services Code of Practice and Cross Sectoral Guidance Notes – **Adopted**			