AGENDA ITEM NO. 7(6)

POLICY & RESOURCES SCRUTINY COMMITTEE – 21 JULY 2009

SUBJECT: **TREASURY MANAGEMENT & CAPITAL FINANCING PRUDENTIAL INDICATORS OUTTURN 2008-09 REPORT**

REPORT BY: **DIRECTOR OF CORPORATE SERVICES**

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1. PURPOSE OF REPORT

1.1 To present Members with details of Treasury Management activities and Capital Financing, together with the related Prudential Indicators for 2008/09.

2. SUMMARY

2.1 The Code of Practice on Treasury Management in the Public Services, which was adopted by the Council on 4th March 2004, sets out a framework of operating procedures, which is encompassed in the Treasury Management Practices (TMPs). The Council subsequently approved the detailed TMPs on 27th May 2004. TMP6 (Reporting Requirements and Management Information Arrangements) provides for the submission of monitoring reports to the appropriate committee on a quarterly basis.

2.2 Under the provisions of the Local Government Act 2003, The Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 [The Capital Regulations], and the CIPFA's "The Prudential Code for Capital Finance in Local Authorities" [the Code], the Authority is obliged to approve and publish a number of indicators relevant to Capital Finance and Treasury Management.

2.3 The Authority's Annual Investment Strategy and Capital Financing Prudential Indicators for 2008/09 were approved by Council on 28th February 2008.

3. LINKS TO STRATEGY

3.1 The report has links to the four basic strategic themes of the Council, taking into account cross-cutting issues where relevant. It has specific links to the effective and efficient application and use of resources.

4. THE REPORT

Treasury Management

4.1 Background – Interest Rates

At the time that the strategy for 2008/09 was decided, the Bank Rate was 5.25% with the Government balancing concerns over the build up of inflationary pressures and the declining growth in GDP. However, in early April 2008, the rate was decreased to 5.00% and Sector's view was that the rate would be maintained throughout most of the year, decreasing to 4.75% by the end of the year. The disruption in the financial markets due to the collapse of Lehman Brothers bank in the U.S., and the Icelandic Banks resulted in concerns shifting to recession, depression and deflation. As a result, the MPC cut rates by 0.50% on 9th October with further cuts following which brought the Bank Rate to 0.50% by March.

Against this background the PWLB 45-50 year rate started the year at 4.43% and was then generally within a band of 4.3 - 4.6% until mid October when there was a peak to 4.84% followed by a dip to 3.86% in early December. Further peaks of 4.84% and 4.72% occurred in late January and early February with the year closing out at 4.58%.

4.2 Borrowing

The Annual Strategy for 2008/09 set out that

- rescheduling opportunities should continue to be evaluated
- new borrowing should average **4.50%**.

4.3 New Borrowing

The final borrowing requirement for 2008/09 of £17.544m was made up as follows:

- replacement of maturing PWLB loans £7.082m
- funding of 2008/09 capital programme £10.462m.

During August new loans totalling £6.5m were raised for 49.50 years at 4.39% with a further £7.5m raised in early October for 50 years at 4.36%. As a result of the financial crisis with the subsequent impact on interest rates (short-term investment rates were falling in line with Bank Rate) and the decision to withdraw from the money market and to invest only in the Debt Management Office (DMADF) and other local authorities in order to minimise risk, it was decided that it would be more prudent and cost effective to fund the balance of the capital programme from maturing investments. Therefore, the balance of the borrowing requirement of some £3.544m was not raised. A summary of new loans is shown in ***Appendix 1 –Table 1.***

4.4 Rescheduling

The Council has engaged Sector Treasury Services to provide specialist advice with regard to Treasury Management activities. One of the areas where the expertise of external Treasury Consultants is of particular benefit is the identification of rescheduling opportunities – the premature repayment/replacement of existing loans to achieve revenue savings and/or the reduction of the Council's average rate of borrowing.

In 2008/09, there were few occasions when opportunities arose to reschedule PWLB loans. However, an opportunity arose in January and PWLB loans totalling some £32.924m were prematurely repaid (no replacement loans were taken for the reasons mentioned in para. 4.4). A summary of loans prematurely repaid is shown in ***Appendix 1 –Table 2*****.**

4.5 Investments

The Annual Strategy for 2008/09 set out that:

- the in-house team would manage all short-term investments in accordance with the Treasury Policy
- short-term investments should achieve, or better, a target rate of **5.00%**

4.6 Short-term Investments – up to 364 Days

Throughout the year the in-house team managed investments averaging £107.46m. The return on these investments, which ranged from short-fixed to 364 days, was 5.09% compared with the target of 5.00%. The amount of interest earned on these investments (excluding interest due but not received from Icelandic banks) was some £5.255m compared with the original estimate of £4.003m.

4.7 Long-term Investments

During December 2008 £10m of these investments matured. The decision was taken not to reinvest in long-term investments due to the uncertainty in the financial markets and therefore the sum was utilised for cashflow purposes. The balance of long-term investments as at 31/03/09 was £10m with a yield of 5.23%.

4.8 A table detailing the full Treasury Management portfolio of loans and investments is shown in ***Appendix 2.***

Prudential Indicators

4.9 Capital Financing Requirement

The capital financing requirement measures the authority's underlying need to borrow for a capital purpose. In accordance with best professional practice, the authority does not associate borrowing with particular items or types of expenditure. In practice, the raising and repaying of loans is determined primarily by professional / expert advice, and may not necessarily take place in the relevant year. In order to create an operating environment within which the Treasury Manager can legitimately react to appropriate advice, the various authorised limits as identified in ***Appendix 3*** are set at a level in excess of the capital financing requirement. During the year, the authority operated within the approved limits.

Appendix 4 shows the value of the Capital Financing Requirement as at 31st March 2009, based on the unaudited Balance Sheet position, is calculated to be £245.968m.

4.10 Prudential Indicators – "Prudence"

The Prudential Indicators for Treasury Management have, in the main, remained unchanged from those detailed in the Annual Strategy 2008/09 report presented to Council in February 2008. Prudential indicators are shown in ***Appendix 3***. The authority is currently operating within approved limits.

4.11 Prudential Indicators – "Affordability"

There is a requirement to analyse and report the capital financing costs, and express those costs as a percentage of the net revenue streams of the authority. These are identified ***Appendix 4*** attached.

Financing costs to net revenue stream

General Fund - the unaudited out-turn, shows a marginal reduction on the previously forecast position. This is mainly attributable to the lower than expected interest rates on borrowing and over achievement of the investment income budget, in spite of the economic downturn.

HRA

The ratio is marginally lower mainly as a result of a higher net revenue stream together with a reduction in interest rates.

Incremental effect of capital investment

General Fund

As a result of delays in a number of capital projects, there is a marginal decrease arising from a lower than expected use of capital receipts to fund actual expenditure and reduction in interest rates.

HRA

There is a marginal reduction in this measure as a result of the reduction in interest rates.

4.12 Capital Expenditure and Funding

Capital Expenditure is reported in ***Appendix 5***, for information purposes. The table indicates the unaudited position as at 31st March 2009 compared to the forecast reported in February 2008. More detail will be reported in due course.

5. FINANCIAL IMPLICATIONS

5.1 This report deals with financial matters.

6. PERSONNEL IMPLICATIONS

6.1 There are no personnel implications

7. RECOMMENDATIONS

7.1 Members are asked to note the report

8. REASONS FOR THE RECOMMENDATIONS

8.1 Compliance with the CIPFA “Code of Practice for Treasury Management in the Public Services”.

9. STATUTORY POWER

9.1 Not applicable

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Cllr. J. Taylor – Chairman, Policy & Resources Scrutiny Committee
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Background Papers:
Treasury Management Working Papers – Accountancy Section.
CIPFA “Code of Practice for Treasury Management in the Public Services”
The Local Government Act 2003
Local Authorities (Capital Finance and Accounting) (Amendment) (Wales) Regulations 2004