MUNICIPAL YEAR 2010/2011 REPORT NO. **50A**

MEETING TITLE AND DATE:
Cabinet
15 September 2010
Council
22 September 2010

REPORT OF:
Director of Finance and
Corporate Resources

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Agenda – Part: 1	Item: 11
Subject: **ANNUAL TREASURY MANAGEMENT OUTTURN REPORT 2009/10 & REVISED INVESTMENT STRATEGY 2010/11** Wards: All	
Cabinet Member consulted: Cllr. A. Stafford	

1. EXECUTIVE SUMMARY

1.1 This report reviews the activities of the Council's Treasury Management function over the financial year ended 31 March 2010.

1.2 The report makes recommendations to extend the Council's investment criteria to allow specified investments up to 364 days. This change if adopted will allow the Council to earn better rates of return on its investments.

1.3 The key points of the report are highlighted below:

		See section:
Debt Outstanding at year end	• *Debt Outstanding unchanged at £220m*	***6***
Interest on new borrowing in year	• *No new external borrowing during the year. All capital borrowing financed by internal resources*	***7***

2. RECOMMENDATIONS

2.1 That Council approves the Treasury Outturn report. .

2.2 To approve changes to the 2010/11 investment criteria as set out in Appendix 2.

3. BACKGROUND

3.1 The Council adopted the CIPFA Revised Treasury Management Code of Practice and approved the annual Treasury Management Policy Statement in February 2010.

3.2 The statement requires the Director of Finance & Corporate Resources to report on the preceding year's treasury management activities. In accordance with best practice, the Director's report includes information about borrowing levels and costs, as well as the impact of the cash flow management arrangements on the Council's financial position.

4. NATIONAL CONTEXT

4.1 Following the economic recession that extended into early 2009, there were reports of a tentative recovery. The Bank of England forecast UK growth to fall by 3.9% in 2009, whilst inflation was forecast to be heading lower and staying lower for longer. The depth of the recession was borne out by the 5.9% year-on-year fall in GDP recorded at the end of the second quarter of 2009. The service sector - the dominant element of UK economy - also stalled for much of early 2009 despite a number of optimistic surveys to the contrary. The first signs of recovery were finally evident in the final quarter of 2009 with growth registering 0.4% for the quarter.

4.2 In order to stimulate growth, the Bank of England maintained the Bank Rate at 0.5% throughout the year. The Bank also took extreme measures on an extraordinary scale to revive the economy through its Quantitative Easing (QE) programme. Financed by the issuance of central bank reserves QE was initially announced at £75bn, and then extended in stages to £200bn.

5. THE HERITABLE BANK IMPAIRMENT

5.1 The major impact on Enfield in 2008/09 was the failure of the Heritable Bank in which the Authority had £5 million invested. This investment was made on 9th January 2008 for 364 days. On 7th October 2008 its parent bank Landsbanki went into administration after the Icelandic government withdrew support for the Icelandic banking system. This meant the Heritable Bank was also forced into administration.

5.2 The Council has been vigorously chasing recovery of our funds and have lodged claims with the Heritable as well as their parent bank. Since this time the Authority has received regular distributions over the year as set out below.

Table 1: Dividends on heritable Bank	**Pence in the p**	**£000s**
Dividend paid on 28 July 2009	16.30	839
Dividend paid on 16 Dec 2009	12.66	659
Dividend paid on 30 March 2010	6.19	322
Total received to date	**35.15**	**1,820**

5.3 In July 2010 the Authority received a further dividend of 6.27p taking the total recovered to £2.146m (43%). The administrator has indicated a further distribution will be made in October.

5.4 The latest estimate from the Administrator has indicated that based on the present economic climate the Council can expect to receive 85% of its claim by 2012.

5.5 The Council's external auditors Grant Thornton have reviewed the Council's Treasury management arrangements and found that the Council had sound arrangements in place and has taken positive and appropriate action to deal with the fall out from the Icelandic banking crisis.

6 BORROWING IN 2009/10

6.1 No new debt was taken out during the year as set out in table 2

6.2

Table 2: Movement in year	**Debt 1 April 2009**	**Debt Repaid**	**New Debt Raised**	**Debt 31 March 2010**
	£000	**£000**	**£000**	**£000**

- Secondly, using the Council's own resources to finance the 2009/10 programme has meant that investments have fallen. Hence the level of risk of counterpart default has been reduced.

6.4 No temporary borrowing was undertaken during the year.

7. INTEREST ON TOTAL DEBT OUTSTANDING

7.1 The average rate paid on total external debt was 5.51% in 2009/10 (5.51% in 2008/09).

7.2 Table 3 shows the interest paid (i.e. the cost of borrowing) by the Council during the year: The fall in interest costs relates to the fact that a £20 million reduction was made last year (November 08) where debt with a coupon rate of 4.5% was repaid prematurely, this was financed by a reducing the level of investments. This gave a full year net saving of 700K.

Table 3: Cost of Borrowing	**2009/10**	**2008/09**
	£000	**£000**
Public Work Loan Board loans (PWLB)	10,005	10,727
Commercial Loans	2,143	2,143
Total Interest on Debt	**12,148**	**12,870**
Short Term Loans	0	39
Total interest paid	**12,148**	**12,909**
Interest Premiums	224	224
Total Cost of Debt	**12,372**	**13,133**

8. DEBT MATURITY STRUCTURE

8.1 The Council has 30 loans spread over 50 years with the average maturity being 35 years. This maturity profile allows the Council to spread the risk of high interest rates when debt matures in any one year.

8.2 Table 4 shows the maturity structure of Enfield's long-term debt and the average prevailing interest rates.

Table 4: Profile Maturing Debt	**Debt Outstanding as at 31 March 2010**	**Average Interest Rate**	**Debt Outstanding as at 31 March 2009**	**Average Interest Rate**
Years	**£000**	**%**	**£000**	**%**
Under 1 year	5,000	3.89	-	-

9. DEBT RESTRUCTURING

9.1 Debt restructuring normally involves prematurely replacing existing debt (at a premium or discount) with new loans in order to secure net savings in interest payable or a smoother maturity profile. Restructuring can involve the conversion of fixed rate interest loans to variable rate loans and vice versa.

9.2 No debt restructuring was undertaken during the year. We will continue to actively seek opportunities to re-structure debt over 2010/11.

10. TREASURY MANAGEMENT PRUDENTIAL INDICATORS: 2009/10

10.1 Throughout 2009/10 total loan debt was kept within the limits approved by the Council at its meeting in February 2009 against an authorised limit of £440 million and an operating limit of £340 million. The authorised limit (as defined by the Prudential Code) was set at £440 million as a precaution against the failure, for whatever reason, to receive a source of income e.g. Council Tax. In the unlikely event of this happening, the Council would need to borrow on a temporary basis to cover the shortfall in cash receipts. In practice it is the operating limit by which the Council monitors its borrowing; any significant breach must be reported to Council.

10.2 The Council held no variable interest rate debt during 2009/10. The Council's Prudential Code however does allow for up to 25% of the debt to be held in variable interest rate debt.

11. INVESTMENTS

11.1 The Council manages its investments arising from cash flow activities in-house and invests within the institutions listed in the Authority's approved lending list. It invests for a range of periods, from overnight to up to five years dependent on the Authority's cash flow, the limits set out in the Prudential Code and the interest rates on offer. The Council also acts as the treasury manager for the 79 Enfield schools within the HSBC banking scheme. The Council produces a three year cash flow model (based on daily transactions) which projects the cash flow movements of the Council linked into the Council's medium term financial plan. This allows the Treasury Management team to make more informed decisions on borrowing and lending decisions.

11.2 In 2009/10 the Council received £2.6 million in interest on money lent out to the money markets, see table 5.

Table 5: Interest Receipts	2009/10	2008/09

11.4 Table 6 shows the maturity structure of Enfield's investments and the prevailing interest rates. This table dramatically shows the change in investment strategy in 2009/10 as a result of the uncertainty within banking, Maturity durations were set at a maximum of three months and there was a very restricted list of authorised financial institutions as seen in Appendix 1.

Table 6: Maturing Investments	**Investments as at 31 March 2010**	**No of Deals**	**Investments as at 31 March 2009**	**No of Deals**
Months			**£000**	
On demand	44,150	3	13,600	1
Within 1 month	20,000	4	19,500	5
Within 3 Months	10,000	2	41,000	8
Within 6 Months	-		24,000	4
Within 9 Months	-		15,000	3
Within 12 Months	-		-	-
Over 12 Months	-		5,000	1
	74,150	**9**	**118,100**	**22**

11.5 The Treasury Management team achieved an average interest rate of 1.89%, out-performing the benchmark (Inter-Bank 7-day lending rate) by 1.49%. This was achieved by adopting an active treasury policy.

11.6 The average rate of interest earned by the average local authority in 2009/10 (based on the CIPFA benchmarking club) was 1.86%. Enfield's average interest rate 1.89%. The benchmarking exercise also showed the cost of the treasury team to be in the lowest quartile demonstrating Enfield to be very cost effective

11.7 The Council's net borrowing increased in 2009/10 as Table 7 demonstrates. The increase on net borrowing reflects the fact that the Authority took the decision to fund the 2009/10 capital programme internally which meant that the level of investments have fallen while external borrowing has remained unchanged. It should also be noted during the year that cash held on behalf of the Pension Fund has been separated from the Council's accounts and is now not included in the Council's investments. In 2008/09 this figure stood at £12.million. This has also contributed to the fall in investments.

Table 7: Trend in Net Borrowing	**2005/06**	**2006/07**	**2007/08**	**2008/09**	**2009/10**

12. EXTENSION TO THE 2010/11 INVESTMENT CRITERIA

12.1 The Council approved the 2010/11 investment criteria in February 2010.

12.2 The Council's new treasury consultants Arlingclose (appointed in April 2010) have reviewed our investment strategy and have recommended that we make the following changes. The main change to the current strategy is extend the period for a termed deposit out to 364 days. This will allow a greater ability to place funds for longer periods and hence afford the opportunity to access higher interest rates.

12.3 The revised criteria is set out in **Appendix 2**

13. ALTERNATIVE OPTIONS CONSIDERED

13.1 None, this report is required to comply with the Council's Treasury Management Policy statement, agreed by Council in February 2003.

14. REASONS FOR RECOMMENDATIONS

14.1 To inform the Council of Treasury Management performance in the financial year 2009/10 and to extend the Council's list of approved bank in order to spread risk

15. COMMENTS OF THE DIRECTOR OF FINANCE & CORPORATE RESOURCES

15.1 **Financial Implications**

Financial implications are implicit in the body of the report.

15.2 **Legal Implications**

The Council has a statutory duty to ensure the proper administration of its financial affairs and a fiduciary duty to tax payers to use and account for public monies in accordance with proper practices.

The Statement has been prepared in accordance with the CIPFA Code of Practice.

15.3 **Key Risks**

Extending the maximum period of deposits will increase the level of risk of default. This fact must be considered against backdrop that investments will still be

16.3 Strong Communities

The recommendations in the report fully accord with this Council priority.

17. PERFORMANCE MANAGEMENT IMPLICATIONS

17.1 The report provides clear evidence of sound financial management, efficient use of resources, promotion of income generation and adherence to Best Value and good performance management.

Background Papers:

Treasury Management Strategy & Policy Report 2010/11

2009/10 CIPFA benchmarking club

APPENDIX 1: INVESTMENTS OUTSTANDING AT 31ST MARCH 2010

	Maturity Date	£	Interest Rate
Call Accounts			
RBS	On demand	19,500,000	0.8%
Money Market deposits			
Goldman Sachs	On demand	10,000,000	0.45%
Standard Life	On demand	14,650,000	0.45%
Deposits			
Lloyds Banking Group	April 2010	5,000,000	1.1%
Lloyds Banking Group	April 2010	5,000,000	1.0%
Lloyds Banking Group	April 2010	5,000,000	1.14%
Lloyds Banking Group	May 2010	5,000,000	1.12%
Nationwide Building Society	May 2010	5,000,000	6.25%
Salford City Council	April 2010	5,000,000	0.5%
TOTAL INVESTMENTS OUTSTANDING AT 31ST MARCH 2010		**74,150,000**	

Appendix 2: Revised Investment Criteria.

Conditions in the financial sector have begun to show signs of improvement, albeit with substantial intervention by government authorities. In order to diversify the counterparty list, the use of comparable non-UK Banks for investments is now considered appropriate.

The sovereign states whose banks are to be included are Australia, Canada, Finland, France, Germany, Netherlands, Switzerland and the US. These countries, and the Banks within them have been selected after analysis and careful monitoring of:

- Credit Ratings (minimum long-term A+)
- Credit Default Swaps
- GDP; Net Debt as a Percentage of GDP
- Sovereign Support Mechanisms / potential support from a well-resourced parent institution
- Share Price

The Council has also taken into account information on corporate developments and market sentiment towards the counterparties. The Council and its Treasury Advisors, Arlingclose, will continue to analyse and monitor these indicators and credit developments on a regular basis and respond as necessary to ensure security of the capital sums invested.

We do remain in a heightened state of sensitivity to risk. Vigilance is key. This modest expansion of the counterparty list is an incremental step. In order to meet requirements of the revised CIPFA Treasury Management Code, the Council is focusing on a range of indicators (as stated above), not just credit ratings.

The maximum period for any investment meeting the above criteria is 364 days.

Limits for Specified Investments are set out in **Appendix 3**