

**NORTH LINCOLNSHIRE COUNCIL**

**AUDIT COMMITTEE**

**QUARTERLY TREASURY MANAGEMENT AND STRATEGY REPORT 2012/13**

**1. OBJECT AND KEY POINTS IN THIS REPORT**

- 1.1 To provide a regular review of the treasury strategy approved each year by council.
- 1.2 This is a report on treasury management performance up to March 2013. The report explains how the strategy has been implemented to date, and the response to changing conditions in financial markets.
- 1.3 The report also provides an update on our Icelandic investments.

**2. BACKGROUND INFORMATION**

- 2.1 The **investment strategy for 2012/2013** aims to reduce risk by
  - Investing for shorter periods up to six months
  - Only investing in UK institutions with a minimum of an adequate credit rating or equivalent
  - Applying a maximum investment limit of £5m for most counter-parties
  - Applying a maximum limit to financial groups rather than separate institutions
  - Removing any foreign institutions from the counterparty list.
- 2.2 The **borrowing strategy for 2012/2013** aims to
  - Suspend external borrowing in the plan period for as long as is prudent
  - Track the differential between short-and long-term interest rates to determine when it is prudent to resume borrowing
  - Borrow only to support the capital programme
  - Maximize borrowing through the PWLB while this gives best value for money
  - Borrow for shorter periods if cash flow requires and
  - Consider debt rescheduling.
- 2.3 The council's budget was framed against the state of financial markets at that time and prospects for the year ahead. This included a Bank of England Base Rate of

0.5% since 5 March 2009. Most economists' expectations were that rates would remain at this all-time low until 2013. It is now expected that low rates will continue for some years to come.

- 2.4 The budget also projects an average cost of external borrowing of 5% from the Public Works Loans Board in later years when internal borrowing is no longer an option, based on a mix of borrowing terms; and sets a range of prudential indicators which the Director of Policy & Resources monitors. This target rate is still achievable should the council decide to borrow.

### 3. **OPTIONS FOR CONSIDERATION**

- 3.1 The report considers the implementation of an agreed strategy. There are therefore no options to consider.

### 4. **ANALYSIS OF OPTIONS**

#### **Investment strategy**

- 4.1 Markets have been volatile with recurring and still ongoing concerns about

- Poor economic recovery resulting in both the UK and Europe facing minimal growth or further recession
- The ability of governments to sustain the burden of debt culminating in the possibility of one or more euro-zone periphery countries being forced to leave the single currency
- The likely turmoil and uncertainty this would cause, and the implications for the solvency of the banking sector.

Most recently this has been reflected in the UK's loss of its AAA status with one of the rating agencies (Moody's), and the banking crisis in Cyprus.

- 4.2 Therefore the focus of cash management has been to maximise security and liquidity. Cash is currently being held in a range of call accounts with UK banks, on short (1 month maximum) deposit with building societies who maintain an adequate credit rating or as short-term (6 month maximum) investments with other local authorities and the Debt Management Office. The approved list of banks and building societies with whom we can make investments, together with their current ratings are shown at Appendix 2.
- 4.3 All investments due to be realised during the period were returned with interest or reinvested. At the end of March outstanding investments were £15m; details are shown in appendix 1 and 1A.
- 4.4 The council has now completed the process of transferring from NatWest to Barclays for the provision of banking services. From 1 April 2013 the investment limits with Barclays will be £10m and £5m for RBS/NatWest.
- 4.5 The historically low base rate means returns on investments continue to be very modest, an average of 0.57% achieved in 2012/13 year to date against a base rate in the same period of 0.5% and a budget target of a similar level.

Nonetheless the current forecast is that investment income will overachieve by £50k in 2012/13, which reflects a higher level of balances than expected through the year.

### **Borrowing strategy**

- 4.6 In line with the approved strategy, there has been no new borrowing to finance the capital programme and internal borrowing has continued to give best value for money. This is the fifth year in which the council has used cash balances to fund capital investment and the saving on debt costs has been factored into the budget.
- 4.7 Scheduled debt repayments continue and have reduced debt outstanding to £108.9m as at March 2013.
- 4.8 Key performance indicators have been updated to reflect the latest phasing of the capital programme:

| Key Indicator  | 2012/13 Target | 2012-13 Estimate |
|--|----------------|------------------|
| (i) Estimates of Capital Expenditure   | £47.17m        | £30.29m          |
| (ii) General Fund ratio of financing costs to the net revenue stream % (based on Prudential Code 2011) | 7.77%          | 8.11%            |
| (iii) Estimated Capital Financing Requirement  | £164.74m       | £157.59m         |

- Indicator (i); There has been further slippage in the capital programme, in particular in the Building Schools for the Future and other school building programmes and a slower take up of schemes approved for funding through the Regional Growth Fund.
- Indicator (ii); The slippage of £7.4m of grant and external funding has reduced the level of the net revenue stream however financing costs which relate to capital spend in earlier financial years have not reduced to the same extent. The ratio remains below the 10%-12% level set at Council on 21<sup>st</sup> February 2012.
- Indicator (iii); The fall in the level of capital expenditure in 2012-13 has reduced the underlying need to borrow to finance capital expenditure by £7.7m. The impact of this reduction is reflected in the capital financing requirement.

### **Icelandic Investments**

- 4.9 Recovery of funds placed with Icelandic banks before October 2008 is progressing well. So far the council has received repayment of £3.69m which is 66.49% of the councils claim. Total recovery is currently estimated to be £5.03m which represents 90.6%. Dividends continue to be received from both Heritable and Landsbanki.

| <b>Institution</b> | <b>Claim</b> | <b>Paid</b> | <b>Estimated Recovery</b> |
|--------------------|--------------|-------------|---------------------------|
| Heritable          | £3.52m       | £2.72m      | £3.00m                    |
| Landsbanki         | £2.03m       | £0.97m      | £2.03m                    |
|                    | £5.55m       | £3.69m      | £5.03m                    |

## 5. RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY, IT)

5.1 The projected revenue cost of financing debt is within budget. A positive outcome is still expected on the return of Icelandic investments as around three quarters of the investment in Heritable Bank has now been realised, and almost half of the Landsbanki investment now recovered.

5.2 The agreed treasury strategy aims to minimise risk to the council finances from any further instability in financial markets.

## 6. OUTCOMES OF INTEGRATED IMPACT ASSESSMENT (IF APPLICABLE)

6.1 Not applicable.

## 7. OUTCOMES OF CONSULTATION AND CONFLICTS OF INTERESTS DECLARED

7.1 Not applicable.

## 8. RECOMMENDATIONS

8.1 That the Audit Committee consider the assurance provided by this report on the effectiveness of arrangements for treasury management, and;

8.2 That the Audit Committee notes the treasury management performance for the period.

DIRECTOR OF POLICY & RESOURCES

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### Background Papers used in the preparation of this report

LAAP Bulletin 82 'Guidance on the impairment of deposits with Icelandic banks', CIPFA –

Treasury Management in the Public Services. Code of Practice and Cross-Sectoral Guidance Notes: Fully Revised Second Edition 2009.

CIPFA –The Prudential Code for Capital Finance on Local Authorities; Fully Revised Second Edition 2009

**APPENDIX 1****INVESTMENT POSITION AS AT 31 MARCH 2013**

| <b>CALL ACCOUNT BALANCES</b>  | £                     |                   |
|---|-----------------------|-------------------|
| Barclays Bank plc Call Account  | 3,963,000             | On call           |
| Bank of Scotland Plc Call Account (Lloyds TSB Group)                        | 973                   | On call           |
| HSBC Bank Plc Call Account  | 20,024                | On call           |
| National Westminster Bank Plc Special Interest Bearing Account              | 9,899,236             | On call           |
| <br><b>OTHER INVESTMENTS</b>  |                       |                   |
| Heritable Bank Limited  | 795,936               | In administration |
| Landsbanki Islands  | 1,055,923             | In receivership   |
| <br><b>SUB-TOTAL</b>  | <br><b>15,735,091</b> |                   |
| <br><b>LESS:</b>  |                       |                   |
| Impairments brought to account in 2011/12 relating to Icelandic Investments | 752,422               |                   |
| <br><b>TOTAL</b>  | <br><b>14,982,669</b> |                   |

## APPENDIX 1A

### INVESTMENTS MADE AND REALISED BETWEEN 01/01/13 AND 31/3/13

| INVESTMENT INSTITUTION                             | DATE INVESTED | AMOUNT    | STATUS/DUE DATE OF PAYMENT |
|--|---------------|-----------|----------------------------|
|  |               | £         |                            |
| <b><u>INVESTMENTS MADE FROM 1 JANUARY 2013</u></b> |               |           |                            |
| Coventry Building Society                          | 02/01/2013    | 2,000,000 | Repaid                     |
| Coventry Building Society                          | 02/01/2013    | 3,000,000 | Repaid                     |
| Coventry Building Society                          | 09/01/2013    | 2,000,000 | Repaid                     |
| Coventry Building Society                          | 09/01/2013    | 3,000,000 | Repaid                     |
| Coventry Building Society                          | 16/01/2013    | 5,000,000 | Repaid                     |
| Coventry Building Society                          | 23/01/2013    | 5,000,000 | Repaid                     |
| Coventry Building Society                          | 30/01/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 30/01/2013    | 3,000,000 | Repaid                     |
| Coventry Building Society                          | 01/02/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 06/02/2013    | 3,000,000 | Repaid                     |
| Coventry Building Society                          | 13/02/2013    | 3,000,000 | Repaid                     |
| Coventry Building Society                          | 15/02/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 20/02/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 20/02/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 20/02/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 22/02/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 25/02/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 01/03/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 04/03/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 05/03/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 07/03/2013    | 2,000,000 | Repaid                     |
| Coventry Building Society                          | 08/03/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 11/03/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 15/03/2013    | 1,000,000 | Repaid                     |
| Coventry Building Society                          | 18/03/2013    | 1,000,000 | Repaid                     |
| Debt Management Office                             | 03/01/2013    | 1,000,000 | Repaid                     |
| Debt Management Office                             | 03/01/2013    | 3,000,000 | Repaid                     |
| Debt Management Office                             | 09/01/2013    | 1,000,000 | Repaid                     |
| Debt Management Office                             | 11/01/2013    | 1,000,000 | Repaid                     |
| Debt Management Office                             | 11/01/2013    | 1,213,000 | Repaid                     |
| Debt Management Office                             | 15/01/2013    | 4,320,000 | Repaid                     |

|                             |            |           |        |
|-----------------------------|------------|-----------|--------|
| Debt Management Office      | 16/01/2013 | 1,162,000 | Repaid |
| Debt Management Office      | 17/01/2013 | 250,000   | Repaid |
| Debt Management Office      | 18/01/2013 | 1,385,000 | Repaid |
| Debt Management Office      | 15/02/2013 | 1,325,000 | Repaid |
| Debt Management Office      | 19/02/2013 | 1,000,000 | Repaid |
| Debt Management Office      | 20/03/2013 | 1,000,000 | Repaid |
| Nationwide Building Society | 03/01/2013 | 1,000,000 | Repaid |
| Nationwide Building Society | 07/01/2013 | 2,000,000 | Repaid |
| Nationwide Building Society | 07/02/2013 | 2,000,000 | Repaid |
| Virgin Money Plc            | 02/01/2013 | 1,500,000 | Repaid |
| Virgin Money Plc            | 02/01/2013 | 1,500,000 | Repaid |
| Virgin Money Plc            | 09/01/2013 | 1,500,000 | Repaid |
| Virgin Money Plc            | 09/01/2013 | 1,500,000 | Repaid |
| Virgin Money Plc            | 16/01/2013 | 3,000,000 | Repaid |
| Virgin Money Plc            | 23/01/2013 | 2,000,000 | Repaid |
| Virgin Money Plc            | 04/02/2013 | 1,000,000 | Repaid |
| Virgin Money Plc            | 05/02/2013 | 1,500,000 | Repaid |
| Virgin Money Plc            | 12/02/2013 | 500,000   | Repaid |
| Virgin Money Plc            | 15/02/2013 | 1,500,000 | Repaid |
| Virgin Money Plc            | 22/02/2013 | 1,000,000 | Repaid |
| Virgin Money Plc            | 04/03/2013 | 1,000,000 | Repaid |
| Virgin Money Plc            | 11/03/2013 | 1,000,000 | Repaid |
| Virgin Money Plc            | 11/03/2013 | 500,000   | Repaid |
| Virgin Money Plc            | 15/03/2013 | 1,500,000 | Repaid |
| Virgin Money Plc            | 18/03/2013 | 1,500,000 | Repaid |

Counterparties Meeting the Councils Investment Criteria 2012/13

|                           |                                       | FITCH RATING |      | MOODY'S RATING |        | STANDARD & POOR'S |      |
|---------------------------|---------------------------------------|--------------|------|----------------|--------|-------------------|------|
|                           |                                       | ST           | LT   | ST             | LT     | ST                | LT   |
| <b>Banks</b>              |                                       |              |      |                |        |                   |      |
|                           | Bank of Scotland Plc                  | F1           | A    | P-1,           | A2,    | A-1               | A    |
|                           | Barclays Bank Plc                     | F1           | A    | P-1,           | A2,    | A-1               | A+   |
|                           | Co-operative Bank PLC                 | F2           | BBB+ | P-2,           | A3     |                   |      |
|                           | HSBC Bank PLC                         | F1+          | AA-  | P-1,           | AA3,   | A-1+              | AA-  |
|                           | National Westminster Bank Plc         | F1           | A    | P-2,           | A3,    | A-1               | A    |
|                           | Northern Rock (Asset Management ) Plc | WD           | WD   | P-1,           | (P)A1, | A-1               | A    |
|                           | Santander UK Plc                      | F1           | A    | P-1,           | A2,    | A-1               | A    |
|                           | Lloyds TSB Bank PLC                   | F1           | A    | P-1,           | A2,    | A-1               | A    |
|                           | Royal Bank of Scotland                | F1           | A    | P-2,           | A3,    | A-1               | A    |
|                           | Standard Chartered Bank               | F1+          | AA-  | P-1,           | A1,    | A-1+              | AA-  |
|                           | Virgin Money PLC                      | F3           | BBB  |                |        | A-2               | BBB+ |
| <b>Building Societies</b> |                                       |              |      |                |        |                   |      |
|                           | Coventry Building Society             | F1           | A    | P-2,           | A3,    |                   |      |
|                           | Leeds Building Society                | F2           | A-   | P-2,           | A3     |                   |      |
|                           | Nationwide Building Society           | F1           | A+   | P-1,           | A2,    | A-1               | A+   |
|                           | Yorkshire Building Society            | F2           | BBB+ | P-2,           | Baa2,  | A-2               | A-   |