APPENDIX 1

Report of the Director of
Policy & Resources

Agenda Item No: 4
Meeting 15 July 2014

NORTH LINCOLNSHIRE COUNCIL

COUNCIL

TREASURY MANAGEMENT AND INVESTMENT STRATEGY ANNUAL REPORT 2013/14

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

1.1 This is a report on treasury performance in 2013/14. The benchmark for measuring performance is the treasury strategy which the council set at its meeting on 19 February 2013.

1.3 The report covers
- The legal and regulatory framework
- How the council performed
- The latest position on our investments

1.4 The key points are that the council

- Has made more longer term investments, within the 6 month limit
- Generated an average return of 0.5% for the year
- Again deferred borrowing for the capital programme
- Kept the total cost of borrowing below 10% of revenue stream
- Completed its recovery of sums invested with Icelandic banks.
- Completed the transfer from the RBS group to Barclays as our primary banker.

2. **BACKGROUND INFORMATION**

The legal and regulatory framework

2.1 The annual treasury management and investment strategy was prepared in line with
- CIPFA Code of Practice in the Public Service Fully Revised 2011
- CIPFA The Prudential Code Fully Revised Second Edition 2011
- DCLG Guidance
- Local Government Act 2003

2.2 The code of practice requires that full Council receive a report on treasury management strategy at the start of the financial year, at mid-year and at year end. The Audit Committee receives progress reports at each meeting and an annual report on the outturn position.

2.3 It also requires the Council to maintain suitable Treasury Management Practices (TMPs), setting out the manner in which the organisation will seek to achieve its Treasury Management policies and objectives, and prescribing how it will manage and control those activities. As part of this ongoing process the Treasury Management Practices adopted by the Council are reviewed on a regular basis.

3 OPTIONS FOR CONSIDERATION

3.1 There are no options for consideration. However the performance against the approved strategy can be evaluated. The annual strategy covers:

- the investment strategy
- the borrowing strategy
- and the prudential indicators for external debt and treasury management.

The Strategy for 2013-14

3.3 The strategy for 2013/14 was based on the council's views on interest rates and appropriate counterparties for investment and borrowing based on experience, market intelligence including that provided by credit rating agencies, brokers, advisors and the financial press.

The key projections were:

- An average bank base rate of 0.5%
- An average loan rate of 4%

The Investment Strategy

3.4 The Investment strategy for 2013-14 aimed to reduce risk by;

- Investing for shorter periods up to six months
- Only investing directly 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
- Investing in a wider range of institutions through a Money Market Fund.

(see Appendix 1 for list of approved counterparties)

The Borrowing Strategy

3.5 The Borrowing Strategy for 2013-14 aimed to;

- Suspend 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
- Maximise borrowing through the PWLB while this gives best value for money
- Borrow for shorter periods if cash flow requires and
- Consider debt rescheduling.

How the council performed

3.6 It should be noted that investments made during this year were set against an improving global economic environment with a greater degree of optimism, and increased levels of certainty regarding the future stability of market conditions.

This allowed us to employ a still prudent, but slightly less cautious approach within the requirements of the strategy, although all investments were still considerably less than the 6 months allowed within the strategy. This degree of caution was still considered necessary to maximise security and liquidity of council funds.

3.7 The key investment statistics follow with further detail at appendix 2:

- Greater use has been made of a Money Market Fund during this year, with 27% of all investments being made using this vehicle.
- 25% of all investments made were placed in instant access call accounts held with high street banks.
- The remaining 48% of investments were made on a fixed term basis.
- Throughout the year the vast majority of these investments were kept reasonably short, with 88% of all fixed rate investments being for 31 days or less.
- The average fixed term investment period was 16 days, with the maximum duration of investment being 92 days.
- To maximise the security of our investments extensive use has been made throughout the year of investing with highly rated building societies (33% of all fixed term investments), highly rated banks (21%) and the UK Debt Management Office [DMO](46%).
- No investments were made directly in foreign banks.
- Investments were made in building societies only where they met the same minimum credit rating applied to bank investments.
- To reduce risk, where institutions were given a negative rating watch or were under review for possible downgrade, no new investments were made if the resulting rating would then be likely to fall below the minimum criteria.
- The average balance invested was £37.9m.
- This was in the form of 335 separate investments totalling £474m.
- Generating an average return of 0.5% for the year compared to a target of average base plus 0.1% i.e. 0.6%. The return reflects the risk averse investment strategy, together with a trend by the major institutions to reduce the rates being offered in their call accounts.
- The closing investment balance was £17.21m, an increase of £1.28m on the starting balance of £15.93m.
- The historically low base rate and the continuing overall emphasis of security over yield has meant that returns on investment have remained low.

3.8 The key borrowing statistics were (also see related performance indicators at appendix 3):

- Overall capital spending of £48.4m against a revised budget of £56.4m.
- Requests for capital programme expenditure rephasing of £8.46m into 2014-15.
- Debt financing costs of 7.32% of revenue stream, below the council's guideline range of 10% - 12%, in part due to the decision to defer new borrowing
- Outstanding debt as at 31 March 2014 was £107.7m, a reduction of £1.2m from the opening position of £108.9m.
- Total debt kept within the authorised and operational boundaries set in the strategy
- And the maturity profile of debt also within the limits set
- No short term borrowing was needed as cash balances remained positive during the year.

3.9 The decision to defer new borrowing for capital purposes continues the practice started in 2008/09. This avoids the short-term cost of paying the differential between the rates at which we can borrow and rate of return on our investment. It makes temporary use of cash balances which would otherwise be exposed to potential loss in volatile financial markets. Between 2008/09 to 2012/13 £71.3m of borrowing was deferred. A further £10.0m has been deferred in 2013/14.

Icelandic Investments

3.10 The council has been working with other local authority creditors of the failed Icelandic Banks to recover the money it invested in 2008. The recovery of Heritable debt has been concluded. The percentage recovery was 94% against a forecast of 85-90%. Further repayments are possible but unlikely. The recovery of the money invested with the Icelandic bank, Landsbanki now known as L.B.I. has also recently been finalised. The council's claim, in conjunction with the majority of other local authority claimants, was sold at auction on 30 January 2014. Overall the council recovered 93% of its investment. This is a very positive outcome.

Institution	Claim	Paid
Heritable	£3.52	£3.31m
LBI (Landsbanki)	£2.03	£1.85m
	£5.55	£5.16m

3.11 This table summarises the impact of Icelandic investments on the council's finances, a total of £5.16m has been recovered from the total claim of £5.55m. The conclusion of recovery of funds has allowed the council to release the impairment provision of £2m into balances to support council spending as part of the 2014/15 budget decision.

4. **ANALYSIS OF OPTIONS**

4.1 This is a report on past performance and there are no options to consider.

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

5.1 The financial implications to this report are covered in section 3.

5.2 Staff time has been effectively dedicated to the gathering of intelligence and the building up of research capacity to aid, sustain and inform the treasury management function in making borrowing and investment decisions. The Council continues to be an active member of the CIPFA Treasury Management Network and to promote staff training.

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 considers 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 2013-14 financial year.

DIRECTOR OF POLICY AND RESOURCES

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Background Papers used in the preparation of this report -

CIPFA Code of Practice in the Public Service Fully Revised 2011
CIPFA The Prudential Code Fully Revised Second Edition 2011
DCLG Guidance
Local Government Act 2003

Appendix 1

COUNTERPARTY LIST 2013/14

BANKS	**Fitch**		**Moody's**		**Standard & Poor's**		**Counterparty Limit**
	ST	**LT**	**ST**	**LT**	**ST**	**LT**	**£**
United Kingdom							
Barclays Bank	F1	A	P1	A2	A-1	A	£10,000,000
HSBC Bank plc	F1+	AA-	P1	AA3	A-	AA-	£5,000,000
Lloyds Banking Group							£5,000,000
Bank of Scotland	F1	A	P1	A1	A-1	A	
Lloyds TSB Bank	F1	A	P1	A1	A-1	A	
RBS Group							£5,000,000
National Westminster Bank	F1	A	P2	BAA1	A-2	A-	
Royal Bank of Scotland	F1	A	P2	BAA1	A-2	A-	
Standard Chartered Bank	F1+	AA-	P1	A1	A-	AA-	£5,000,000
Virgin Money Plc	F2	BBB+					£3,000,000

BUILDING SOCIETIES	**Fitch**		**Moody's**		**Standard & Poor's**		**Counterparty Limit**
	ST	**LT**	**ST**	**LT**	**ST**	**LT**	**£**
Nationwide	F1	A	P1	A2	A-1	A	£5,000,000
Yorkshire	F2	BBB+	P2	Baa1			£3,000,000
Coventry	F1	A	P2	A3			£5,000,000
Leeds	F2	A-	P2	A3			£5,000,000
GOVERNMENT INSTITUTIONS							
Debt Management Office							Unlimited
Local authorities							
District Council's							£3,000,000
All Other LA's							£5,000,000
Fire Authorities							£5,000,000
Police authorities							£5,000,000

NOTE:
Credit Ratings correct at 29 May 2014.

Appendix 2

Investment Record 2013-14

Investments at start and end of year	Limit	01.04.12	31.03.13
	£	£	£
UK Clearing Banks			
Lloyds Banking Group	5,000,000	973	4,967,118
RBS Group	*10,000,000	9,904,857	626,340
Barclays Banking Group	^10,000,000	4,153,137	9,982,280
HSBC Bank PLC	5,000,000	20,024	2,207
Building Societies			
Local Authorities			
Money Market Funds	3,000,000	0	1,631,000
Other Investment Institutions			
Landsbanki Islands	5,000,000	1,055,923	0
Heritable Bank LTD	5,000,000	795,936	0
TOTAL INVESTED		**15,930,850**	**17,208,945**

Other organisations where funds were deposited during the year 2013/14

Coventry Building Society
Debt management Office
Leeds Building Society
Nationwide Building Society
Virgin Money PLC
Yorkshire Building Society

*** Initial limit of £10,000,000 reduced to £5,000,000 once no longer our own bankers**

^ Initial limit of £5,000,000 increased to £10,000,000 once they became our own bankers

Appendix 3

PRUDENTIAL GUIDELINE INDICATORS

	2013/14	2013/14
	Budget	Actual
	£'000	£'000
(i) capital expenditure	56,361	48,370
(ii) General Fund ratio of financing costs to the net revenue stream	7.11%	7.33%
	£'000	£'000
(iii) The capital financing requirement	172,350	160,212
(iv) the authorised limit for external debt including borrowing and other long term liabilities	233,000	233,000
(v) the operational boundary for external debt including borrowing and other long term liabilities	173,000	173,000
	%	%
(vi) upper limit for fixed rate exposure	100	Target Met
(vii) upper limit for variable rate exposure	20	Target Met
(viii) upper and lower limits for maturity structure of borrowing		
UPPER LIMIT		
under 12 months	15	)
12 months and within 24 months	15	)
24 months and within 5 years	50	} Target Met
5 years and within 10 years	75	)
10 years and above	90	)
LOWER LIMIT		
under 12 months	0	)
12 months and within 24 months	0	)
24 months and within 5 years	0	} Target Met
5 years and within 10 years	0	)
10 years and above	25	)
(ix) total principal sums invested for periods longer than 364 days	none	none