AGENDA

ITEM 5

Report to: Audit Committee

Date of meeting: 30 September 2009

Report of: Interim Head of Finance

Title: Treasury Management Performance Report

1.0 SUMMARY

1.1 This report provides a review of the Council's Treasury Management performance for the five months ending 31st August 2009/2010.

2.0 RECOMMENDATIONS

2.1 That the Committee considers the new proposals put forward by CIPFA to changes in its Treasury Management Code highlighted in para 3.3.

2.2 That the Committee notes the Treasury Management Performance for the five months ending 31st August 2009

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3.0 Background

3.1 At its meeting of 30th June 2009 The Committee received a report outlining its Treasury Management and Investment Strategy for 2009/2010, its performance to date for 2009/10 and highlighting the main proposals of the Audit Commission document entitled ''Risk and Return: English Local Authorities and the Icelandic Banks''.

3.2 In Summary the proposals and findings of the Audit Commission Document included:

- 127 authorities were affected (WBC was not one of them).

- Authorities should set the treasury management framework so that the organisation is explicit about the level of risk it accepts and the balance between security and liquidity and the yield to be achieved.

- Authorities should ensure treasury management policies are scrutinised in detail by a specialist committee and are monitored regularly.

- Should train those elected members of authorities who have accountability for the stewardship of public money so that they are able to scrutinise effectively.

- Should use the fullest range of information before deciding where to deposit funds.

3.3 In addition to the Audit Commission, CIPFA are currently consulting on revisions to its Treasury Management Code along the lines of the Audit Commission proposals and going further. The main proposals include :

- The organisation will be expected to name the individual/group of individuals or committee to be responsible for ensuring effective scrutiny of the Treasury Management Strategy and polices

  It is suggested that in Watford BC this would be the Audit Committee

- The annual strategy can be approved by a named relevant committee and does not have to be approved by full Council, if this path is followed then the strategy needs to be reported to full Council

  In Watford the Strategy is currently approved by full Council. Audit Committee Members may wish to consider commenting on the annual strategy prior to approval by full Council

- The responsible officer should ensure that all Council members tasked with Treasury Management responsibilities including those responsible for scrutiny have access to training relevant to their needs and those responsibilities

  Audit Committee Members have previously been given training and further training has been arranged, for this Audit Committee and other interested Members by the Councils Treasury Management Advisors, Sector. Future training will be co-ordinated by the Head of Strategic Finance using both external and internal resources

- In addition to the Annual strategy and year-end operation report a mid year report will be required. This should be presented to full council or relevant committee

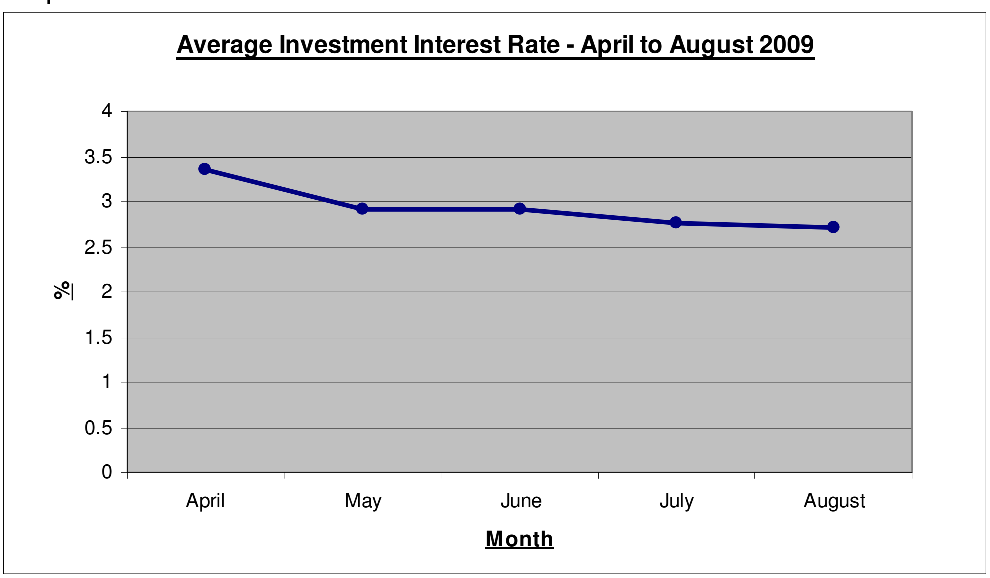
Members have already received a report at its previous meeting and have a further one included here. It is considered that future updates on Treasury Management performance to date will be undertaken on a quarterly basis. Members may wish to consider how the information contained within this report meets their needs

Consultation on the Revision to the CIPFA Treasury Management Code ended on 18th September 2009

4.0 **Treasury Management Performance for 2009/2010**

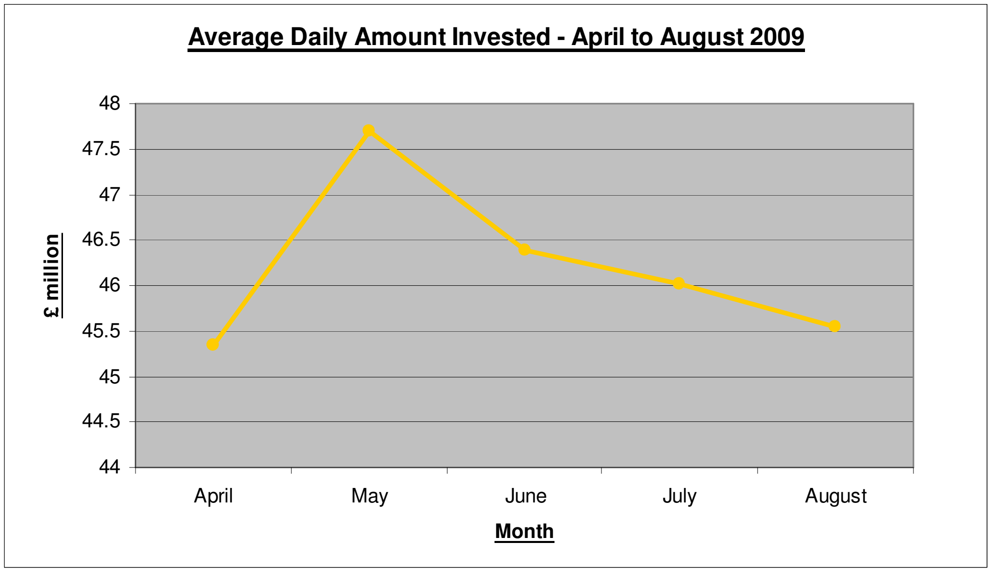
4.1 **Average Investment Rates**

The Council's Treasury Management Policy requires that the performance of the investment portfolio be reported to Members. For the five month period ended 31st August 2009 the average interest rate was 2.72% and the amount of interest earned for the period totalled approximately £520k. This compared to a performance target of 0.1% above the average base rate figure, which was 0.5% for the period. This significant over achievement of 2.2% was by and large due to the timely investment of a number of investments for 12 months back in October 2008 at the highest point of the interest rate curve (6.5%). A track on average interest rate for the period is shown below :



4.2 **Amounts Invested**

At 31st August 2009 the total amount held in Investments totalled £43 million with a further £3 million held in overnight deposits at the Co-Op bank for cash flow purposes. The average daily amount invested for the five-month period ending 31st August 2009 was £45.5 million. There were 10 new deals and 13 maturities in August compared to 6 and 5 respectively for the previous month. The average duration of these deals was 224 days with 4 of the deals being for 1 year in order to lock in at the most favourable rates on the market. The average interest rate on these new deals was 1.54 % with the longer deals earning between 1.6% and 1.8%. A track of average daily amounts invested for the period can be shown as follows :



4.3 **Counterparties**

The Councils Counterparty list (list of institutions that it lends to) as at 31st March 2009 is attached at Appendix A. With the exception of Kent Reliance Building Society and Progressive Building Society, which are soon to mature all other Building Societies are within the top 6 of building societies by asset size. The current strategy aims to achieve a mix of investments held by building societies and banks of 50/50. At the 31st August this stood at 40/60 between banks and building societies respectively. At 15th September this had changed to 60/40.

4.4 **Forecast Of Base Rates**

The Council receives information on bank base rate interest rate forecasts and other Treasury Management information and advice from its appointed Treasury Management advisors Sector. A number of sources give predictions on interest rates as follows :

	Sept 09	Dec 09	Mar 10	June 10	Sep 10	Dec 10
Sector	0.5%	0.5%	0.5%	1.00%	1.5%	2.00%
UBS	0.5%	0.5%	0.5%	0.5%	0.75%	1.00%
Capital Economics	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%

From the predictions above Members will note that bank base rates are not expected to rise until June 2010 the earliest and consequently the return that Members can expect on their investments will in turn remain static. This will ultimately effect the Councils revenue budget which will be discussed later

5.0 Treasury Management Practice for 2009/2010

It is not the intention to formally revise the Treasury Policy for 2009/2010 but nevertheless, in the light of increased instability in the financial markets, the following variations to current policy will be followed some of which were highlighted in the last report to Members:

- No further investments will be made with Irish banks once the current investments have matured

- Previously members were advised that only deals with the top 6 building societies by asset size would be considered. Recent deals using this methodology has limited the council to rates of 0.5% and 0.6% for three month monies. Whereas increasing the counterparty list of building society to the top 10 would increase returns to between 1.5 and 1.9%. Asset size of building societies varies but even the 10th largest building society Norwich and Peterborough has an asset base of approximately £5 billion. Clearly asset size is not always a suitable indicator of financial liquidity as we have seen with the collapse, Dunfermline Building Society, but unless the counterparty list is extended then investment returns to the Council will continue to fall as higher rated investments such as Anglo Irish matures. Recent deals with building societies have been limited to up to 3 months and officers are currently seeking further information from an organisation that examines the financial information on the building society sector in addition to asset base, which it will use before placing further deals with building societies.

- The Council remains open to the use of the Government Debt Management Office due to the restrictive nature of its counterparties but as previously advised the use of this facility will be kept to a minimum wherever possible due to the low investment returns currently around 0.4%.

- The Council will continue to invest in banks that meet its minimum credit ratings although a number of the high street banks are generally not interested in the relatively small amounts that we have to offer or offer derisory rates of interest

- In view of the current prediction in interest rates the Council will continue to place some of its money for longer term (up to 364 days) to benefit from higher rated returns. Currently approximately 48% of its investments are long term, timed to mature when interest rates are predicted to rise. This level of long term investment is justified given a

General Fund Working Balance of £1.7 million and Earmarked and General Reserves of approximately £10.3 million which it is not envisaged will be required to be drawn on in the short term

- The Council continues to be debt free and is likely to remain so for the foreseeable future. Whilst the current strategy allows temporary borrowing no such borrowing was undertaken in the first five months of this financial year.

6.0 **Reappointment of Sector as Treasury Management Advisors**

In July 2008 the Council tendered for its Treasury Management Advisory service, for a three-year period commencing September 2008. The contract was subsequently awarded to Sector Treasury Services Ltd with an extremely competitive bid for an initial period of 12 months with an option to renew for a further period of two years. Officers have found the information and advice provided by Sector to be extremely good value for money and would recommend the extension. The period would align with the current contract that Three Rivers District Council have with their advisors at which stage it is intended that there would be a joint procurement process.

7.0 **Conclusions**

The current market for investments is stable but with base rates continuing to stay low ,investment returns remain low. The Council has benefited from fixed rate deals placed last year at interest rates of 6% but recent returns are no where near this figure and as these investments mature the average rate earned is reduced. Interest earned on new deals varies with the high street banks and larger building societies offering rates on 3 month deals as low as 0.4% with some of the smaller building societies, who are becoming starved of cash offering up to 1.9%.

- The quandary for the Council like most councils is whether to take more risk at the expense of security to gain higher returns. Some authorities have decided not to and invest surplus cash with the Debt Management Office which has seen an unprecedented amount of activity recently, other authorities carry on regardless. Officers believe that the action taken in the period covered by the report to
- increase long term investments,
- increase holdings in main High Street Banks
- work with top 10 building societies by asset base, with more informed market information

enable the authority to make the most from its investments whilst at the same time minimise its exposure and spread risk.

8.0 **IMPLICATIONS**

8.1 **Financial Issues**

The investment interest budget for 2009/10 was set at £1,013,000.

Through the Council's budget monitoring report, The Finance Digest, this has been steadily revised downwards by £100k initially and more recently to £855,000 as higher rated investments mature and are replaced by lower rated ones. The budget has been predicated on an average interest rate of 2.2% and whilst the current average interest earned is 2.72% this average will continue to fall as higher rated investments mature and are replaced with lower rated new deals of between 0.6% and 1.9% highlighted ion paragraph 5 above.

8.2 **Legal Issues** (Monitoring Officer)
The Head of Legal and Property Services comments that there are statutory limitations governing cash fund investments and all proposals within this report ensure continued compliance.

8.3 **Potential Risks**

Potential Risk	**Likelihood**	**Impact**	**Overall score**
Investment with non approved body	2	3	6
Failure to achieve investment interest budget targets	3	3	9
Those risks scoring 9 or above are considered significant and will need specific attention in project management. They will also be added to the service's Risk Register.			

8.4 **Staffing**

8.4.1 None Directly

8.5 **Accommodation**

8.5.1 None Directly

8.6 **Community Safety**

8.6.1 None Directly

8.7 **Sustainability**

8.7.1 None Directly

<u>Background Papers</u>

CIPFA Treasury Management Code of Practice
Audit Commission publication-Risk and Return
Treasury Management Policy, Practice and Strategy (reported to this Committee on 19th January 2009

<u>File Reference</u>
None