

Subject:	Treasury Management Policy Statement 2012/13 (including Annual Investment Strategy 2012/13) – Mid Year Review		
Date of Meeting:	29 November 2012		
Report of:	Acting Director of Finance		
Contact Officer:	Name: Peter Sargent	Tel: 29-1241	
	E-mail: peter.sargent@brighton-hove.gov.uk		
Wards Affected:	All		

FOR GENERAL RELEASE

1. SUMMARY AND POLICY CONTEXT:

- 1.1 The Treasury Management Policy Statement 2012/13 (TMPS) and the Treasury Management Practices (including the schedules) for the year commencing 1 April 2012 were approved by Cabinet on 15 March 2012. Full Council approved the Annual Investment Strategy 2012/13 (AIS), which forms part of the TMPS, on 22 March 2012. The policy statement sets out the key role for treasury management, whilst the practices and schedules set out the annual targets for treasury management and the methods by which these targets shall be met. The AIS sets out the parameters within which investments can be made.
- 1.2 The purpose of this report is to advise of the action taken during the period April to September 2012 to meet the policy statement and practices and the investment strategy.

2. RECOMMENDATIONS:

- 2.1 That Policy & Resources Committee endorses the action taken during the half-year to meet the Treasury management policy statement and associated treasury management practices and the Annual investment strategy.
- 2.2 That Policy & Resources notes the maximum indicator for risk agreed at 0.05% has not been exceeded.
- 2.3 That Policy & Resources notes the authorised limit and operational boundary set by the Council have not been exceeded.

3. RELEVANT BACKGROUND INFORMATION/CHRONOLOGY OF KEY EVENTS:

Overview of markets

- 3.1 The half-year has seen a continuation of the financial uncertainty within the Euro zone, with its consequent impact on business and consumer confidence in the UK and other major economies. In the UK the bias of policy decisions by the

Bank of England (BoE) continued towards stimulating the economy with official rates remaining at ½% and quantitative easing (QE) increasing to £375 billion. Other measures designed to increase bank lending to businesses have been introduced by the BoE. Despite these measures consumer confidence remains relatively low and growth is modest.

3.2 Inflation has fallen from earlier highs but UK economic growth remains stalled, with a fall in gross domestic product falling for a third quarter in succession. Interest rates are projected to remain low for the foreseeable future thereby impacting on investment returns.

3.3 A commentary on the markets is set out in Appendix 1 to this report.

Treasury management strategy

3.4 A summary of the action taken in the six months to September 2012 is provided in Appendix 2 to this report. The main points are:

- § long-term debt remained unchanged at £207.8m, with no new long-term debt raised or repaid during the half-year;
- § no short-term debt has been raised in the half-year;
- § the level of investments made by the in-house treasury team as at 30 September 2012 totalled £67.9m, an increase of £39.8m during the half-year;
- § the level of investments made by the cash manager as at 30 September 2012 totalled £24.9m, an increase of £0.2m during the half-year;
- § the return on investments by the in-house treasury team and cash manager has significantly exceeded the target rate;
- § the two borrowing limits approved by Budget Council in February 2012 – the ‘authorised limit’ and ‘operational boundary’ – have not been exceeded in the first half of the year.

3.5 Treasury management activity in the half-year has focused on a short-term horizon as summarised in the table below.

	Amount invested 1 April to 30 Sept 2012			
	Fixed deposits	Money market funds	Total	
Up to 1 week	£143.2m	£74.3m	£217.5m	62%
Between 1 week & 1 month	£49.1m	-	£49.1m	14%
Between 1 month & 3 months	£79.0m	-	£79.0m	23%
Over 3 months	£2.8m	-	£2.8m	1%
	£274.1m	£74.3m	£348.4m	100%

3.6 Minimising capital risk on the investment portfolio continues to be the primary objective for the council’s investment strategy. The investment counterparty list approved by the Council in March 2012 reflected low risk investment parameters. These parameters were relaxed marginally in July 2012 to include financial institutions with “good” as well as “excellent” credit quality. The decision to relax the parameters was taken in response to a general downgrading of major banks and high levels of surplus funds. Over three-quarters of the investments made in the half-year were for 1 month or less. The average period for fixed deposits (i.e. excluding money market funds) was around 18 days. The average amount

invested in money market funds was £27.9 million.

- 3.7 On 25 June officers and members met with Sector (the council's external treasury advisors) to review the ethical investment options available for council investments and to consider changes to the counterparty list included in the AIS in light of the current conditions in the financial markets. The outcome of the meeting was reported to Policy & Resources Committee on 12 July.

Ethical investments

- 3.8 In terms of ethical investment options Sector identified a number of alternatives but in the main these require investors to deposit funds for periods between 2-5 years. Returns over the short-term for these options can be extremely volatile, potentially resulting in loss of capital. Given the council's current investment strategy to invest only short-term effectively ruled out these options for the time being.
- 3.9 Other short-term investment options were considered, including increasing investment with the Cooperative Bank (as council banker) and investment in banks with a strong ethical strategy. Members agreed that these options increased the potential risk to the investment portfolio to an unacceptable level and therefore no further action has been taken.
- 3.10 Sector advised that the council is considered to be at the forefront of promoting an ethical investment statement for cash deposits and the statement is often passed by Sector to other local authorities seeking similar investment objectives. The council will continue to promote socially responsible investments.

Investment counterparties

- 3.11 During the half-year the rating agencies downgraded a substantial number of financial institutions on the council's list of approved counterparties resulting in lower limits, reduced periods and, in some cases, suspension from the list. The review in June identified a number of potential changes to the investment strategy which were aimed at increasing the number of counterparty options.
- 3.12 Details of the changes to the 2012-13 Annual Investment Strategy are set out in the July report to this Committee. In summary the changes involved:
- allowing investment in financial institutions incorporated within the UK and regulated by the Financial Services Authority rather than UK only institutions,
 - increasing limits on investment with financial institutions that have received Government support (i.e. part nationalised banks);
 - a relaxation in the minimum rating from "highest" credit quality to "good" credit quality.
- 3.13 The above changes, which were approved by full Council on 19 July, introduced a number of new institutions to the approved list. Details of these are included within Appendix 2 along with a summary of investments made.

Summary of treasury activity April to September 2012

- 3.14 The table below summarises the treasury activity in the half-year to September 2012 with the corresponding period in the previous year.

	Apr to Sep 11	Apr to Sep 12
Long-term borrowing repaid	(£6.0m)	-
Short-term borrowing repaid	-	-
Investments made	£292.8m	£348.4m
Investments maturing	(£294.0m)	(£308.6m)

- 3.15 The following table summarises how the day-to-day cash flows in the second half-year have been funded compared to the same period in the previous year.

	Apr to Sep 11	Apr to Sep 12
Cash flow surplus	£4.8m	£39.8m
Decrease in long-term borrowing	(£6.0m)	-
Decrease in short-term borrowing	-	-
Decrease / (increase) in investments	£1.2m	(£39.8m)

Security of investments

- 3.16 A summary of investments made by the in-house treasury team and outstanding as at 30 September 2012 is tabled below. The table shows that investments continue to be held in good quality, short-term instruments.

	Balance o/s 30 Sept 2012	
Government backed institutions	£14.0m	21%
'AAA' rated funds	£25.9m	38%
'A' rated institutions	£19.6m	29%
'BBB' rated institutions	£8.4m	12%
	£67.9m	100%
Period – less than one week	£30.1m	44%
Period – between one week and one month	£19.7m	29%
Period – between one month and three months	£18.1m	27%
	£67.9m	100%

Risk

- 3.17 As part of the investment strategy for 2012/13 the Council agreed a maximum risk indicator of 0.05%. The indicator is a simple target that measures the risk within the investment portfolio based on counterparty risk and length of investment. The indicator set for 2012/13 is consistent with the investment parameters set out in the AIS.
- 3.18 The following table summarises the maximum indicator for each month in the half-year period and confirms investments have been made in good to high quality counterparties.

	Apr 12	May 12	Jun 12	Jul 12	Aug 12	Sep 12
Maximum risk indicator	0.005%	0.006%	0.005%	0.002%	0.004%	0.005%

Performance

- 3.19 The following table summarises the performance on investments compared with the budgeted position and the benchmark rate.

(*) Annualised rates	In-house investments		Cash manager investments	
	Average balance	Average rate (*)	Average balance	Average rate (*)
Budget 2012/13 – full year	£36.5m	0.88%	£24.6m	1.05%
Actual to end Sept 2012	£63.2m	0.80%	£24.8m	1.50%
Benchmark rate (i.e. average market rate) to end Sept 2012	-	0.44%	-	0.44%

4. CONSULTATION

- 4.1 The council's external treasury advisors have been consulted in the drafting of this report. No other consultation was undertaken.

5. FINANCIAL & OTHER IMPLICATIONS:

Financial Implications:

- 5.1 The financial implications arising from the action taken under the TMPS are included in the Financing Costs budget. The month 6 forecast for Financing Costs shows an overspend of £350,000. Of this £375,000 is a direct result of the change in the way the HRA is financed. This effectively means there is an underspend of £25,000 due to higher interest on other activities.

Finance Officer Consulted: Peter Sargent

Date: 11/10/12

Legal Implications:

- 5.2 Action under the TMPS must be in accordance with Part I of the Local Government Act 2003 and regulations issued thereunder. Relevant guidance also needs to be taken into account.
- 5.3 This report is for information purposes only and as such it is not considered that anyone's rights under the Human Rights Act will be adversely affected by it.

Lawyer Consulted:

Abraham Ghebre-Ghiorghis

Date: 10/10/12

Equalities Implications:

- 5.4 There are no direct implications arising from this report.

Sustainability Implications:

- 5.5 There are no direct implications arising from this report.

Crime & Disorder Implications:

- 5.6 There are no direct implications arising from this report

Risk & Opportunity Management Implications:

- 5.7 The continuing uncertainty in the financial markets means the increased risk in lending has not abated. The action taken in the first six months of 2012/13 has resulted in the council reducing capital risk on its investment portfolio.
- 5.8 The position will be regularly monitored and, when confidence returns to the financial markets, opportunities to raise new borrowing and rebuild the investment portfolio will be considered.

Corporate / Citywide Implications:

- 5.9 Investment income is used to support the budget requirement for the council. Any action taken to reduce the risk of capital loss will have a downward impact on the level of interest received.

6. EVALUATION OF ANY ALTERNATIVE OPTION(S):

- 6.1 This report sets out action taken in the six months to September 2012. No alternative options are therefore considered necessary.

7. REASONS FOR REPORT RECOMMENDATIONS

- 7.1 The TMPS requires the Director of Finance to report on the action taken by the council in meeting borrowing limits and investment parameters after the first 6 months and at the end of the financial year. This report fulfils the first reporting requirement.

SUPPORTING DOCUMENTATION

Appendices:

1. Market Overview – April to September 2012
2. A summary of the action taken in the period April to September 2012
3. Performance and balances

Documents In Members' Rooms

None

Background Documents

1. Part I of the Local Government Act 2003 and associated regulations
2. The Treasury Management Policy Statement and associated schedules 2012/13 approved by Cabinet on 15 March 2012
3. The Annual Investment Strategy 2012/13 approved by full Council on 22 March 2012
4. Treasury Management Policy Statement 2011/12 (including Annual Investment Strategy 2011/12) – End of year Review approved by Policy & Resources Committee on 12 July 2012 and Council on 19 July 2012
5. Papers held within Strategic Finance, Finance
6. The Prudential Code for Capital Finance in Local Authorities published by CIPFA 2011

