

**CABINET**  
**15 JULY 2009**

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**ANNUAL REPORT ON TREASURY MANAGEMENT 2008-09**

**Executive Summary**

In accordance with the CIPFA Prudential Code for Capital Finance in Local Authorities 2003 (The Prudential Code), the Council adopted a Treasury Management Strategy (TMS) for 2008-09, including a set of Prudential Indicators (PrIs) and an Annual Investment Strategy (AIS) at its meeting on 22 January 2008. This report shows how the Council has performed against this strategy.

**Proposal**

The Cabinet is asked to consider and note:

- a) the actual cash position at the end of 2008-09 against the original forecast for the year;
- b) PrIs and other treasury management strategies set for 2008-09 against actual positions resulting from actions within the year as detailed in Appendix A; and
- c) investments during the year in the context of the Annual Investment Strategy as detailed in Appendix B.

**Reasons For Proposals**

To give members of the Cabinet an opportunity to consider the performance of the Council against the parameters set out in the last approved Treasury Management Strategy.

This report is required by the Prudential Code for Capital Finance in Local Authorities and the CIPFA Code of Practice for Treasury Management in the Public Services.

MARTIN DONOVAN  
Chief Finance Officer

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**ANNUAL REPORT ON TREASURY MANAGEMENT 2008-09**

**Background & Purpose of Report**

1. In accordance with the CIPFA Prudential Code for Capital Finance in Local Authorities 2003 (The Prudential Code), the Council adopted a Treasury Management Strategy (TMS) for 2008-09, including a set of Prudential Indicators (PrIs) and an Annual Investment Strategy (AIS) at its meeting on 22 January 2008.
2. An interim report was submitted to Cabinet on 16 December 2008 for the period from 1 April to 30 September 2008. This report covers the whole financial year ended 31 March 2009.

**Main Considerations for the Cabinet**

3. This report reviews:
  - a) the actual cash position at the end of 2008-09 against the original forecast for the year;
  - b) PrIs and other treasury management strategies set for 2008-09 against actual positions resulting from actions within the year (see Appendix A); and
  - c) investments during the year in the context of the Annual Investment Strategy (see Appendix B).

**Review of cash position**

4. In setting strategies and PrIs for 2008-09, a forecast cash position for the year was prepared based on expected inflows and outflows of cash during the year.
5. The actual cash position at 31 March 2009 is a cash requirement of £17.7 million, against an anticipated cash requirement of £30.0 million. The variation of £12.3 million, which relates to both capital and revenue items, is mainly a result of grant income levels being in excess of those anticipated.

6. The main reasons for the variation between forecast and budgeted cash flows are as follows:

<b>Reason for variance in deficit</b>	<b>Variance £ million</b>
Grants and Other Income	+36.1
Pension Fund Advances and Refunds	+13.1
Change in Working Capital/Other Cash Movements (e.g. changes in debtors, creditors, other provisions and liabilities)	<u>-36.9</u>
<b>Total variance</b>	<b><u>+12.3</u></b>

7. There were no opportunities to restructure PWLB loans in 2008-09 due to, both, interest rates at the appropriate maturity profiles and the high level of premiums payable for the early repayment of PWLB loans.
8. A new one year PWLB loan of £5 million was taken up in October 2008, 'freeing up' surplus cash to invest short term.

#### **Review of Prudential Indicators and Treasury Management Strategy for 2008-09**

9. The detail of the review is given in Appendix A. The Cabinet is asked to note that:
- a) all action has been within the agreed PrIs;
  - b) the average interest rate for long term debt is 4.29%, compared to 4.30% in 2007/08;
  - c) short term cash deficits and surpluses were managed through temporary loans and deposits with a return on investments of 4.58% (6.52% in 2007-08, the reduction reflects the decrease in the level of interest rates since October 2008) in comparison to a market rate of 4.49%, based on the Average 3 Month LIBID Rate for 2008/09 (London Interbank Bid rate, i.e. the rate at which banks are prepared to borrow from other banks); and
  - d) no cost effective opportunity arose to obtain increased investment returns within acceptable risk levels from investment in Money Market Funds and/or with External Cash Managers.

#### **Review of Investment Strategy**

10. This review is detailed in Appendix B. The Cabinet is asked to note that:
- a) all action was within the agreed Annual Investment Strategy; and
  - b) no long term investment opportunities were identified.

## **Risks Assessment and Financial Implications**

11. The primary treasury management risks to which the County Council is exposed are adverse movements in interest rates and the credit risk of its investment counterparties.
12. Investment counterparty risk is controlled by criteria for assessing and monitoring the credit risk of borrowers as authorised by the Annual Investment Strategy. Appendix B of this report details action taken in 2008-09.
13. At 31 March 2009, the Council's average interest rate of long term debt was 4.29%, which, according to the latest available information, remains one of the lowest rates amongst UK local authorities.
14. It is also considered important to ensure that there is an even spread of loans and avoid the prospect of too many loans maturing in any one year, which may need to be replaced when interest rates are high. A summary of the present maturity profile is shown in Appendix C (i).
15. Having sufficient flexibility in the Council's strategy has enabled the Council to retain a reasonable balance between the costs of borrowing and return on investments. The investment rate of return for the year was 4.58%, against an average borrowing rate of 4.29%.

## **Equalities Impact of the Proposal**

16. None have been identified as arising directly from this report.

## **Legal Implications**

17. None have been identified as arising directly from this report.

## **Reasons for Proposal**

18. To give members of the Cabinet an opportunity to consider the performance of the Council against the parameters set out in the last approved Treasury Management Strategy.
19. This report is required by the Prudential Code for Capital Finance in Local Authorities and the CIPFA Code of Practice for Treasury Management in the Public Services.

## **Environmental Impact of Proposal**

20. None have been identified.

## **Proposal**

21. The Cabinet is asked to consider and note:
  - a) the actual cash position at the end of 2008-09, which was £12.3 million better than the original forecast for the year;

- b) Prls and other treasury management strategies set for 2008-09 against actual positions resulting from actions within the year as detailed in Appendix A; and
- c) investments during the year in the context of the Annual Investment Strategy as detailed in Appendix B.
- d) the average rate of return on investments during the year was 4.58% against an average borrowing rate of 4.29%.

MARTIN DONOVAN  
Chief Finance Officer

Report Author: Keith Stephens

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The following unpublished documents have been relied on in the preparation of this Report: NONE

**REVIEW OF PRUDENTIAL INDICATORS FOR 2007-08**

1. Where appropriate the figures shown in this report are consistent with future years' estimated PrIs, which were reviewed and reported as part of the 2008-09 budget process.

***Prl 1 - Capital Expenditure***

2. The table below shows the original and revised estimate of capital expenditure against the actual for the year 2008-09:

	<b>2008-09 Original Estimate £ million</b>	<b>2008-09 Revised Estimate £ million</b>	<b>2008-09 Actual Outturn £ million</b>
Capital Expenditure	99.5	98.5	71.7

3. The Capital Programme has been actively managed throughout the year, including a number of reprofiling. The revised capital budget (capital outturn position for 2008-09) is £76.0 million. Other details are as reported in the capital outturn report presented to the Cabinet at its meeting on 23 June 2009.

***Prl 2 – Ratio of Financing Costs to Net Revenue Stream***

4. Prl 2 expresses the net costs of financing as a percentage of the funding receivable from the Government and council tax payers. The net cost of financing includes interest and principal repayments for long and short term borrowing, as well as other credit-like arrangements, netted off by interest receivable in respect of cash investments.

	<b>2008-09 Original Estimate</b>	<b>2008-09 Revised Estimate</b>	<b>2008-09 Actual</b>
Financing Costs as a percentage of Revenue Budget	6.5%	5.8%	5.6%

5. The actual is below the revised estimate due to increased investment income.

***Prl 3 – Estimate of Incremental Impact of Capital Investment Decisions on the Council Tax***

6. This indicator is relevant during budget setting, as it reflects the impact on the Band D Council Tax caused by any agreed changes in the capital programme.

***Prl 4 – Net Borrowing and the Capital Financing Requirement***

7. Prl 4 measures the so called “Golden Rule” which ensures that over the medium term net borrowing is only for capital purposes. The table below shows the original and revised estimate for 2008-09 compared with the actual position at the year end.

	<b>2008-09 Original Estimate £ million</b>	<b>2008-09 Revised Estimate £ million</b>	<b>2008-09 Actual £ million</b>
Capital Financing Requirement	231.3	237.8	233.4
Net Borrowing	134.6	139.3	131.1
<b>Capital Financing Requirement not funded by net borrowing</b>	<b>96.7</b>	<b>98.5</b>	<b>102.3</b>

8. The Capital Financing Requirement (CFR) increases whenever capital expenditure is incurred. If resourced immediately (from capital receipts, direct revenue contributions or capital grant/contributions) the CFR will reduce at the same time that the capital expenditure is incurred, with no net increase in CFR.
9. Where capital expenditure is not resourced immediately, there is a net increase in CFR, represented by an underlying need to borrow for capital purposes, whether or not external borrowing actually occurs. The CFR may then reduce over time by future applications of capital receipts, capital grants/contributions or further charges to revenue.
10. This PrI is necessary, because under an integrated treasury management strategy (in accordance with best practice under the CIPFA Code of Practice on Treasury Management in the Public Services), borrowing is not associated with particular items or types of expenditure, whether revenue or capital
11. Net Borrowing is the Council's total external debt less its short term cash investments.

***PrI 5a – External debt***

	<b>31/3/08 Actual £ million</b>	<b>31/3/09 Expected £ million</b>	<b>31/3/09 Actual £ million</b>
Borrowing	189.5	195.3	186.3
Other Long Term Liabilities	0.2	0.2	£0.2
<b>TOTAL</b>	<b>189.7</b>	<b>195.5</b>	<b>186.5</b>

12. This PrI shows the gross External Debt outstanding at year end. The actual borrowing figure is the outstanding long term borrowing as shown in Appendix C (i).
13. Details of all long term loans taken during the year are given in Appendix C (i). As shown, only one new (PWLb) loan was taken out during the financial year.
14. A one year, £5 million loan was taken out at an interest rate of 3.79%. The average rate of all outstanding long term debt was reduced to 4.29% at 31 March 2009.

***Prl 5b – Operational Boundary for External Debt***

<b>Operational Boundary</b>	<b>2008-09 £ million</b>	<b>2009-10 £ million</b>	<b>2010-11 £ million</b>	<b>2011-12 £ million</b>
Borrowing	256.3	302.0	299.2	301.5
Other Long Term Liabilities	0.2	0.2	0.2	0.2
<b>TOTAL</b>	<b>256.5</b>	<b>302.2</b>	<b>299.4</b>	<b>301.7</b>

15. This Prl is for gross borrowing and was set at a limit that would allow the Council to take all its financing requirement as loans, if this was most cost effective. The limit was set to anticipate expected expenditure and has not been exceeded during the period of this report. The maximum gross borrowing during the year being £186.5 million at 31 March 2009.

***Prl 5c – Authorised Limit for External Debt***

<b>Authorised Limit</b>	<b>2008-09 £ million</b>	<b>2009-10 £ million</b>	<b>2010-11 £ million</b>	<b>2011-12 £ million</b>
Borrowing	294.8	347.4	344.0	346.8
Other Long Term Liabilities	0.2	0.2	0.2	0.2
<b>TOTAL</b>	<b>295.0</b>	<b>347.6</b>	<b>344.2</b>	<b>347.0</b>

16. This Authorised Limit was not exceeded at any time during the year, as maximum borrowing was below the lower Operational Boundary.

***Prl 6a – Upper Limit on Fixed Interest Rate Exposures***

**The Council's upper limit for fixed interest rate exposure for the period 2008-09 to 2011-12 is 100% of net outstanding principal sums.**

***Prl 6b – Upper Limit on Variable Interest Rate Exposures***

**The Council's upper limit for variable interest rate exposure is 5% for 2008-09, 22% for 2009-10, 21% for 2010-11 and 21% for 2011-12 of net outstanding principal sums.**

17. All loans and investments are at fixed rates of interest.

***Prl 7 – Maturity Structure of Borrowing***

<b>Limits on the Maturity Structure of Borrowing</b>	<b>Upper Limit</b>	<b>Lower Limit</b>	<b>Actuals 31/3/08</b>
Maturing Period:			
- under 12 months	15%	1%	2.7%
- 12 months and within 24 months	15%	1%	0.0%
- 2 years and within 5 years	45%	8%	0.0%
- 5 years and within 10 years	75%	15%	0.0%
- 10 years and above	90%	40%	97.3%

18. In addition to the main maturity indicators it is considered prudent that no more than 15% of long term loans should fall due for repayment within any one financial year. The actual maximum percentage falling due for repayment in any one year is currently 7.0% (£13 million) in both 2052-53 and 2053-54. The average interest rate on present long-term debt is 4.288%, which, according to the latest available information, is one of the lowest local authority rates.
19. A change has been implemented to the treatment of market (LOBO – Lender Option, Borrower Option) loans, where maturity dates are now based on the contractual life of the loan rather than the first option (call) date, which accords with the Statement of Recommended Practice (SORP) 2008 and current guidance.
20. This has resulted in breaches in one of the upper limits of the maturity structure of borrowing (10 years and above) and three of the lower limits. The higher limit will be reviewed and options considered during 2009-10. The lower limits have since been amended to 0% as approved by the County Council at its meeting on 24 February 2009 as part of the Treasury Management Strategy 2009-10 (Report VII of the Budget Booklet) as recommended by the Implementation Executive at its meeting on 11<sup>th</sup> February 2009.

***Prl 8 – Total Principal Sums invested for periods longer than 364 days***

21. This Prl is covered by the Annual Investment Strategy, which is detailed in Appendix B.

***Prl 9 – Compliance with CIPFA Code of Practice for Treasury Management in the Public Services***

<p><b>The Council is and will continue to be fully compliant with the CIPFA Code of Practice for Treasury Management in the Public Services.</b></p>
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22. This Code of Practice has been complied with during 2008-09.

**Other Treasury Management issues**

***Short Term Cash Deficits and Surpluses***

23. It was agreed that temporary loans and deposits would be used to cover short term cash surpluses and deficits that would arise during the year. Such borrowing or investments would be made to specific dates at fixed rates, with reference to the cash flow requirements. No investments in Money Market Funds were made during the year.
24. The temporary loans and deposits used are summarised in Appendix C (ii).

***Longer Term Cash Balances***

25. When available for investment it was placed on short term deposits, as no significant advantage could be gained by placing out on longer term investment.

**INVESTMENT STRATEGY FOR 2008-09**

1. All investments of surplus cash balances were placed to ensure:
  - a) the security of capital, deposits only being placed with financial institutions which met the **high credit ratings** laid down in the approved Strategy;
  - b) the liquidity of investments, all deposits being placed for fixed periods at fixed rates of interest; and
  - c) all such investments were in sterling and in “Specified Investments”, as prescribed in the DCLG Guidance on Local Government Investments (the “Guidance”).
2. As summarised on Appendix C (ii), 368 deposit transactions were processed during the year, with a gross value of £822.993 million. Of deposits placed, 137 were placed direct with HSBC Bank Treasury on the Council’s overnight deposit account and 231 were placed with other borrowers.
3. Details of the deposits outstanding at the end of the year, totalling £58.351 million, are shown in Appendix C (ii). These deposits represent the Council’s reserves both long term, such as the PFI and Insurance funds, and short term such as creditors or payments in advance.
4. No investments were made in Money Market Funds during the year.
5. The County Council contracts with a treasury adviser, regularly reviewing credit ratings of potential organisations and their respective country’s ratings, together with other ‘tools’ used to assess the credit quality of institutions such as credit default swaps. The Council uses this information to assess institutions with which it may place deposits or from which it may borrow, including interest rate forecasts for both borrowing and investment, together with setting a ‘benchmark’ borrowing rate. The Council’s investment policy is ‘aimed’ at the prudent investment of surplus cash balances to optimise returns whilst ensuring the security of capital and liquidity of investments. However, as with the recent experience of Icelandic bank investments, the Council, like any other organisation, can be exposed to financial risk.

**SUMMARY OF LONG TERM BORROWING 1 APRIL 2008 - 31 MARCH 2009**

**LOANS RAISED During the Period**

<b>Date raised</b>	<b>Lender</b>	<b>Amount (£m)</b>	<b>Type</b>	<b>Interest rate (%)</b>	<b>Maturity date</b>	<b>No. of years</b>
October	PWLB	5.000	Maturity	3.790	Oct-09	
	<b>Total</b>	5.000				

**Average period to maturity (years)**

**0.00**

**Average interest rate (%)**

**3.79**

\* Loans taken to restructure debt

\*\* Loans taken for purchases instead of leasing

**Maturity Profile at 31 March 2009**

<b>Year</b>	<b>Amount (£m)</b>	<b>%age</b>	<b>Average rate (%)</b>
1 to 5 years	5.102	2.7	4.303
6 to 15 years	0.032	0.0	4.452
16 to 25 years	25.623	13.8	4.603
26 to 50 years	155.500	83.5	4.412
Over 50 years	0.000	0.0	-
<b>Totals</b>	186.257	100.0	4.288

**Average period to maturity (years)**

**37.55**

**SUMMARY OF TEMPORARY LOANS AND DEPOSITS 1 April 2008 - 31 March 2009****Deposits Outstanding at 31 March 2009**

Borrower	Amount £m	Terms	Interest rate(%)
HSBC	0.850	No fixed maturity date	0.3500
Ulster Bank Ltd	4.000	Fixed to 01-May	5.7800
Bank of Scotland	5.000	Fixed to 19-Jun	6.7500
Coventry Building Society	3.000	Fixed to 01-Apr	0.4100
Emirates Bank International	3.000	Fixed to 01-Apr	0.7000
City of Birmingham Council	4.000	Fixed to 09-Apr	0.5500
Emirates Bank International	5.000	Fixed to 17-Apr	0.9500
Barclays Bank	10.000	Fixed to 30-Apr	0.8500
National Bank ABU Dhabi	3.000	Fixed to 20-Apr	0.6000
Bank of Scotland	2.501	No fixed maturity date	0.7500
Alliance & Leicester	5.000	No fixed maturity date	0.8000
Clydesdale Bank	5.000	No fixed maturity date	0.8000
Heritable Bank	3.000 *		6.0000
Heritable Bank	3.000 *		6.0000
Heritable Bank	2.000 *		6.0000
<b>Total</b>	<b>58.351</b>		

\* Outstanding deposits with Hertible Bank. The amounts are shown as the original deposit placed. These amounts have been impaired in the accounts to reflect the amount likely to be received.

**Transactions During the Period**

Type	Balance 1 Apr 08 £m	Raised		Repaid		Balance 31 Mar 09 £m	Interest variance * high/low(%)
		Value £m	No.	Value £m	No.		
<b>Temporary loans</b>							
- General	0.000	0.000	0	0.000	0	0.000	
Total	0.000	0.000	0	0.000	0	0.000	
<b>Temporary deposits</b>							
- General	69.869	668.353	231	688.721	240	49.501	0.4/6.75
- HSBC Treasury	1.500	154.640	137	155.290	110	0.850	0.25/5
Total	71.369	822.993	368	844.011	350	50.351	

\* Interest variance is the highest/lowest interest rate for transactions during the period