AGENDA ITEM No. 4

NORTH LANARKSHIRE COUNCIL REPORT

To: POLICY & RESOURCES (FINANCE & CUSTOMER SERVICES) SUB-COMMITTEE		Subject: TREASURY MANAGEMENT MONITORING REPORT PERIOD 1 APRIL TO 30 JUNE 2012
From: HEAD OF FINANCIAL SERVICES		
Date: 10 August 2012	Ref: PH/JQ/Q1	

1. Introduction

1.1 The purpose of this report is to inform on the quarterly activity (1 April 2012 to 30 June 2012) of the Council's loans and investment portfolios.

2. Background

2.1 The Council manages its treasury activities in line with the CIPFA Code "Treasury Management in the Public Services'. The Code requires the Council to produce reports on its Treasury Management policies, practices and activities on a regular and on-going basis. The Council fulfils these obligations in part by the preparation of a Treasury Management Monitoring report produced on a quarterly basis contained herein.

2.2 The Treasury activity undertaken in the first quarter of 2012/2013 reflects the key requirements of the Council's 2012/2013 Treasury Management Strategy, with the Public Works Loan Board and Long-term Money Market being the prime source of long-term funds. In addition, long term variable rate loans or temporary loans have not exceeded 25% of total borrowing. In terms of investment activity, all temporary lending is conducted with approved financial institutions.

3. Quarterly Activity

3.1 Summary Position

3.1.1 The net overall borrowing position to 30 June 2012 is shown in Appendix 1. The balance of £745.3m represents a decrease of £11.8m from the position at the 31 March 2012. This reduction was primarily due to repayments of £2.8m in respect of the liabilities outstanding in respect of finance lease and PPP obligations and a reduction in the bank overdraft by £4.6m which represents the level of BACS payments outstanding and cheques unpresented at the 30 June 2012. There was also a rise of almost £4.8m in the level of investment balances held at the end of the quarter, partially offset by an increase of £0.4m in the level of temporary borrowing. Also, as noted in paragraph 3.3.1, short-term borrowing of £17.5m from North Lanarkshire Municipal Bank Ltd was reclassified as long-term.

3.2 Debt Restructuring

3.2.1 During the quarter under review, in conjunction with our Treasury advisors, we monitored the economic climate in relation to our financial targets and Treasury Management strategy. The interest rates prevailing throughout the period resulted in no beneficial opportunities for debt restructuring/rescheduling of the PWLB debt portfolio arising.

3.2.2 Further reports regarding future activity will be presented to Committee as appropriate.

3.3 Borrowing

3.3.1 At 30 June 2012, long term borrowing amounted to £583.2m which represented a rise of almost £17.5m. This reflected the Council agreeing a new mortgage arrangement with North Lanarkshire Municipal Bank Ltd, effectively reclassifying £17.5m from short term to long term borrowing on a variable rate basis, repayable in 5 years, subject to loan conditions being acceptable to both parties.

3.3.2 During this quarter, excluding the new lending arrangement described within the previous paragraph, no other long term borrowing was undertaken, internal cash balances and short term borrowing being used to meet daily revenue account requirements and the capital financing requirement, in lieu of future borrowing for capital purposes. This approach was adopted in light of interest rate expectations, the management of carrying costs and the availability of short term borrowing up to 364 days at attractive rates.

3.3.3 At 30 June 2012, short-term borrowing amounted to £54.8m, which represented a fall of almost £21.7m. As mentioned previously, £17.5m of this reduction is due to the reclassification of a loan from North Lanarkshire Municipal Bank Ltd from short term to long term of borrowing. There was also a reduction in bank overdraft levels by £4.6m as described above offset by a £0.4m increase in temporary borrowing described below.

3.3.4 Throughout the quarter during the normal course of business, day to day cash flow needs were monitored and this resulted in the short term borrowing transactions totaling £20.4m in terms of cash received and £20.0m in cash repaid which resulted in an overall increase of £0.4m by the end of the period. The period of borrowing ranged from 1 month to 364 days, with the Council's liquidity and interest rate risk being managed effectively.

3.4 Short Term Investments

3.4.1 In the first quarter of 2011/2012, positive cashflows enabled short-term investments of £248.9m to be undertaken. During the same period, approximately £244.1m of short-term investments matured. The net effect of these transactions was an increase of £4.8m in investment balances as highlighted in paragraph 3.1.1.

3.4.2 The Council in line with the approved strategy to manage liquidity maintained a minimum balance of £5m available on an overnight basis (instant access) throughout the quarter. This ensured that the Council maintained the necessary prudent level of funds to meet all business/service objectives.

3.4.3 On the 22 June 2012, Moody's, one of the leading rating agencies downgraded the ratings of 15 banks and securities firms with global markets operations, including Barclays plc, the Royal Bank of Scotland Ltd and a number of foreign banks. These ratings downgrades reflected a range of factors, including historical earnings volatility, the weak operating environment in Europe and banks holding very large capital markets business.

3.4.4 The Council's approach to investment strategy and assessment of creditworthiness remains robust, closely monitoring developments and taking the appropriate action to manage the Council's Treasury Management risk. This involved the Council opening a number of money market funds during the quarter, a permitted investment within the Council's investment strategy. These are pooled funds that invest in short-term debt instruments, providing the benefits of pooled investment, with the Council participating in a more diverse and high-quality portfolio than it could individually. As set out in the investment strategy, the Council only invests in those funds that have an AAA-rated stable net asset value within strict credit, diversification and maturity parameters and governed by the Institutional Money Market Funds Association (IMMFA).

3.4.5 Given the recent Moody's ratings changes mentioned in section 3.4.3 above and the associated increased difficulty in finding suitable investment vehicles, approval is sought to increase the money limits for money market funds from a maximum of £20m in total to a maximum of £30m, with the limit per fund of £10m or 0.5% of fund size remaining unchanged as set out in the investment strategy.

3.4.6 During the quarter, the Council purchased a 1 month £5.0m certificate of deposit (CD) from one of the highest rated financial institutions in the world, taking advantage of this type of financial investment instrument being made available on the market for a short time. A CD is a certificate issued from a financial institution that records that the Council has deposited a specified sum of money with a maturity date and a fixed interest rate. The use of CDs was approved as part of the 2012/2013 Investment Strategy.

3.4.7 Overall, the Council demonstrated good performance levels in investment activity during the quarter with the investment rate achieved from investing surplus funds being consistently higher than the 7 day and 1 month LIBID (London Inter-bank Bid Rate) rate, and the Council's Instant Access Account.

3.4.8 The Treasury Management team continues to take a prudent approach to investing surplus funds in line with the approved 2012/2013 Investment Strategy.

3.5 Interest Rate Movements

3.5.1 In the first quarter of 2012, at each of its meetings in April, May and June, the Monetary Policy Committee (MPC) decided to retain the Bank of England base rate at 0.50%.

3.5.2 During the quarter the short term 7 day LIBID rate remained stable around the 0.45% mark with the rate expected to remain on hold for a considerable time as the recovery in the economy remains insipid. Whilst the current economic uncertainty exists and the fragility of the banking sector remains, day to day investment activity is within the short term horizon (less than 3 months) with the main focus being the security of the investment.

3.5.3 Following a similar path to the previous quarter, longer term interest rates fluctuated over the quarter. For example, the PWLB 25 year borrowing rate fell from 4.32% to 4.00% by the end of June being as high as 4.39% in early April, averaging levels of 4.13%. With the Greek debt crisis and the unfolding of tensions within the eurozone, the gilt edged market has been a major beneficiary of the flight of investment funds to safe havens with gilt prices rising and yields falling sporadically during the quarter.

3.5.4 The impact of lower interest rates is that income earned from investing surplus cash balances is reduced but as mentioned earlier the Council continues to demonstrate good performance levels in investment activity.

3.5.5 The Treasury Management Section will continue to monitor financial and economic policy and their impact upon the Council's investment and borrowing activity.

4. The Prudential Code for Capital Finance in Local Authorities

4.1 The Local Government in Scotland Act 2003 requires the Council to undertake its Treasury activities with regard to the Prudential Code for Capital Finance in Local Authorities.

4.2 On 22 February 2012, Committee approved a report titled, "Treasury Management Strategy 2012/2013 and Treasury and Prudential Indicators 2012/2013 to 2014/2015". This report detailed a variety of mandatory and local indicators, aimed at assisting members to determine that proposed capital investment levels and treasury management decisions satisfied the key requirements of affordability, prudence and sustainability. Performance against key prudential indicators is detailed within Appendix 2.

4.3 Committee will wish to note the following salient points:-

(i) Indicator 1(a) illustrates that investment on capital expenditure is anticipated to be higher than set out in February, primarily due to slippage of a number of projects within the 2011/2012 capital programme being carried forward into 2012/2013. This is monitored in detail as part of the Council's capital programme reporting mechanisms. This will result in an increase in the level of borrowing required to meet the capital programme with higher than anticipated revenue contributions offsetting lower than expected capital grants and capital receipts.

(ii) The Prudential Code requires the Council's capital investment to be affordable and prudent. To demonstrate this, a Prudential Margin (the need to borrow versus actual borrowing) is calculated. Indicator 1(b) demonstrates a healthy prudential margin at the 30 June 2012. The net borrowing requirement is lower at this point in time as the Council is in the initial stages of implementing its 2012/2013 capital expenditure programme. The current year capital financing requirement to date has been funded using internal cash balances and short term borrowing, with the timing and profile of the further borrowing managed giving full consideration to liquidity, interest rate and refinancing risk.

(iii) Indicator 2 illustrates that both the overall authorised and operational borrowing limits for borrowing and long term liabilities have not been exceeded, with the maximum borrowing undertaken within the period being well below the approved boundaries.

(iv) Indicator 3(a) sets upper limits on the Council's exposure to the effects of interest rate changes by setting limits for each category of debt held (fixed or variable rate) which subsequently limits the Council's interest payable that is fixed or variable. During the first quarter of 2012/2013, the actual levels remained below the limits for the fixed and variable interest rate exposure limits.

(v) Indicator 3(b) highlights a projected reduction of £2.2m in net loan external interest payments compared to the prudential estimates for 2012/2013. External interest payments show a favourable variance of £2.1m reflecting lower external debt levels carried forward from 2011/2012 due to a reduced borrowing requirement in this year, partially offset by an anticipated increased borrowing requirement in 2012/2013. There is also a revised profile in respect of the timing of new borrowing managing investment security, liquidity and interest rate risk, given the current balances and reserves held and short term borrowing opportunities mentioned previously.

(vi) Yields from investing surplus balances in 2012/2013 are expected to be higher due to average cash balances held being greater than expected and the continuing availability of call accounts offering relatively attractive interest rates from secure financial institutions.

(vii) Indicator 3(c) relates to the level of fixed debt due to mature within time periods. The level of debt maturing remains within the upper limits set for each category at the beginning of the financial year.

4.4 The prudential indicators have remained in accordance with those approved by Committee on 22 February 2012. The projected final outturn illustrates a healthy prudential margin and borrowing levels that are below sustainable limits, ensuring that the projected capital investment levels remain affordable and sustainable.

5. Recommendation

5.1 It is recommended that Committee:

(i) Notes the treasury management activity for the quarter ended 30 June 2012, including the positive performance against the key prudential indicators.

(ii) Approves an increase in the money limits for money market funds from a maximum of £20m in total to a maximum of £30m, with the limit per fund of £10m or 0.5% of fund size remaining unchanged.

Head of Financial Services

For further information please contact Joseph Quinn, Treasury Manager on tel ext 2061.

LOANS , LONG TERM LIABILITIES & INVESTMENTS AS AT 30 JUNE, 2012

APPENDIX 1

	BALANCE 01-Apr-12	DEBT RESTRUCTURING EARLY REDEMPTION	REFINANCING	NEW BORROWING	PRINCIPAL REPAYMENTS	NET CASH MOVEMENTS	BALANCE 30-Jun-12
LONG-TERM LOANS							
PWLB	454,680,806	0	0	0	(28,847)	0	454,651,958
MONEY MARKET LOANS	111,000,000	0	0	0	0	0	0
MUNICIPAL BANK	0	0	0	17,500,000	0	0	17,500,000
	565,680,806	0	0	17,500,000	(28,847)	0	583,151,958
SHORT-TERM LOANS							
TEMPORARY	31,000,000	0	0	20,400,000	(20,000,000)	0	31,400,000
MUNICIPAL BANK	34,396,322	0	0	0	(17,500,000)	0	16,896,322
INTERNAL LOANS	6,280	0	0	0	0	0	6,280
BANK OVERDRAFT	11,047,173	0	0	0	(4,561,773)	0	6,485,400
	76,449,775	0	0	20,400,000	(42,061,773)	0	54,788,002
LONG -TERM LIABILITIES							
FINANCE LEASE OBLIGATIONS	12,307,792	0	0	0	(1,815,299)	0	10,492,492
PPP LONG TERM LIABILITY	144,341,000	0	0	0	(1,021,750)	0	143,319,250
	156,648,792	0	0	0	(2,837,049)	0	153,811,742
TOTAL EXTERNAL DEBT	**798,779,373**	**0**	**0**	**37,900,000**	**(44,927,670)**	**0**	**791,751,703**
INVESTMENTS							
CASH IN HAND	1,121,318	0	0	0	0	(396,366)	724,952
OUTSIDE AGENCIES INCL CALL & TRACKER A/CS	40,437,000	0	0	0	0	4,743,000	45,180,000
CLYDESDALE BANK - INSTANT ACCESS	167,000	0	0	0	0	407,000	574,000
TOTAL INVESTMENTS O/STANDING	**41,725,318**	**0**	**0**	**0**	**0**	**4,753,634**	**46,478,952**
NET BORROWING	**757,054,055**	**0**	**0**	**37,900,000**	**(44,927,670)**	**(4,753,634)**	**745,272,751**

Prudential Code for Capital Finance in Local Authorities

1. Capital Expenditure, Capital Financing Requirement and Prudential Margin

(a) Capital Expenditure

	Initial Estimate 2012/2013 (£000s)	Projected Outturn 2012/2013 (£000s)
Total Spend	120,544	128,448
Financed By:		
Borrowing	71,010	77,532
Capital Receipts	4,045	3,408
Cash Grants	26,816	24,380
Capital from Current Revenue	18,673	23,128

(b) Prudential Margin Calculation

	Initial Estimate 2012/2013 (£000s)	Position as at 30/06/12 (£000s)	Projected Outturn 2012/2013 (£000s)
Capital Financing Requirement	915,278	909,017	909,017
Net Borrowing requirement	843,061	745,273	803,873
Prudential Margin	72,217	163,744	105,144

2) Authorised Limit and Operational Boundary

	Initial Authorised Limit 2012/2013 (£m)	Initial Operational Boundary 2012/2013 (£m)	Maximum Borrowing Level Q1 2012/2013 (£m)
Borrowing	770	760	649.3
Other Long-term Liabilities	165	160	156.6

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a) Interest Rate Exposures

	Upper Limits 2012/2013 (%)	Position as at 30/06/12 (£000s)
Fixed Interest Rates	110.00%	82.27%
Variable Interest Rates	30.00%	17.73%

b) Interest Payments & Income due on Loans Outstanding/Funds Invested

	Initial Estimate 2012/2013 (£000s)	Projected Outturn 2012/2013	Variance (£000s)	%tage
Interest Payable on Fixed Rate Debt	28.4	26.2	-2.2	-7.77%
Interest Payable on Variable Rate Debt	5.8	5.9	0.1	2.50%
Total External Interest Payments	**34.2**	**32.1**	**-2.1**	**-6.03%**
External Interest Receivable	-0.2	-0.3	-0.1	50.00%
Net Loan External Interest Charges	**34.0**	**31.8**	**-2.2**	**-6.36%**

c) Maturity Structure of Borrowing

	<12months	12 months to 2 years	2 to 5 years	5 to 10 years	10 to 20 years	20 to 40 years	>40 years
Upper Limit maturing :Fixed Rate Debt	15.00%	15.00%	25.00%	35.00%	40.00%	40.00%	40.00%
Lower Limit maturing :Fixed Rate Debt	0.00%	0.00%	0.00%	5.00%	5.00%	10.00%	10.00%
Maturity structure at the start of Q1	1.21%	1.51%	10.09%	17.03%	18.72%	26.46%	24.98%
Maturity structure at the end of Q1	2.05%	1.55%	10.12%	21.11%	15.44%	27.40%	22.34%