REPORT TO:	Executive Board Sub-Committee
DATE:	10th September 2009
REPORTING OFFICER:	Operational Director – Financial Services
SUBJECT:	Treasury Management 2009/10 1st Quarter: April – June
WARDS:	Borough Wide

1.0 PURPOSE OF REPORT

1.1 The purpose of the report is to update the Sub-Committee about activities undertaken on the money market as required by the Treasury Management Policy.

1.2 CIPFA issued an interim Treasury Management guidance document in March 2009, highlighting Best Practice recommendations for Local Authorities to follow. The document suggests that members should be informed of Treasury Management activities at least twice a year, but preferably quarterly. This report therefore ensures this Council is embracing Best Practice in accordance with CIPFA's recommendations. It is expected that CIPFA will issue an updated Treasury Management Code of Practice in the autumn of 2009.

2.0 RECOMMENDED: That the report be noted.

3.0 SUPPORTING INFORMATION

3.1 <u>Economic Background</u>

The following has been provided by Sector, the Council's treasury management advisors:

Highlights of the quarter:

- The 'green shoots' of recovery emerge;
- GDP contracted by 2.4% during last quarter, the largest fall for over 50 years, an improvement in the output-related data was to be somewhat expected.
- Monetary policy loosened further via the extension of the Bank of England's quantitative easing programme, but lending growth is still slow;
    - Unemployment rise and earnings growth fall;
    - Inflation fall further, but oil prices rise;
    - Bond yields and equity prices rise in response to the improved economic outlook;
    - Sterling appreciate, but only to a level well below its 2007 peak;

- Activity strengthen to a similar extent in the US, but a much weaker extent in Europe.

The first quarter saw some encouraging signs that the rate of contraction in the economy had eased considerably. Retail sales grew by 1.0% in April, and while they fell back in May, they remained above March's level. Consumer confidence continued to pick up. Industrial production rose by 0.2% m/m in April, the first rise since November 2007, and the Nationwide house price index rose in May and June, leading to the first quarterly rise since Q4 2007.

April's Budget announced an injection of £5.2bn in 2009/10, but a tightening of £5.2bn in 2011/12. The Chancellor forecast that public sector net borrowing would increase to 12.5% of GDP in 2009/10 and that net debt as a percentage of GDP will leap from 41.2% in 2008/09 to 62.9% in 2009/10, before peaking at 94.2% in 2015/16. This may have a significant impact on the UK economy.

After rapidly cutting official interest rates to a record low of 0.5%, the MPC increased the amount of asset purchases under the Bank's quantitative easing (QE) programme from £75bn to £125bn in May. The MPC still retains the option to extend these purchases by a further £25bn before having to ask the Chancellor for further authorisation. However, while QE does at least seem to have been successful in improving liquidity in financial markets, its impact on the real economy remains limited.

Inflationary pressures within the economy continued to reduce in the quarter, although at a slower rate than had been expected. The key factors in this trend are tax rises and increasing oil prices. While the headline rate of CPI inflation fell to 2.2% in May, the reduction was smaller than the consensus expected. RPI inflation fell to -1.1% in May.

3.2 Economic Forecast

The following forecast has been provided by Sector;

	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12
Bank rate	0.50%	0.50%	0.50%	1.00%	1.50%	2.00%	2.50%	3.00%	3.75%	4.25%	4.50%	4.75%
5yr PWLB rate	2.70%	2.75%	2.85%	3.10%	3.30%	3.45%	3.75%	4.00%	4.40%	4.70%	4.85%	5.00%
10yr PWLB rate	3.65%	3.70%	3.70%	3.80%	3.95%	4.15%	4.40%	4.65%	4.85%	5.00%	5.05%	5.20%
25yr PWLB rate	4.40%	4.40%	4.50%	4.50%	4.55%	4.70%	4.80%	4.95%	4.95%	5.10%	5.20%	5.30%
50yr PWLB rate	4.55%	4.55%	4.60%	4.65%	4.75%	4.85%	4.95%	5.05%	5.10%	5.25%	5.25%	5.35%

This indicates that the Bank Rate will remain at an historical low level until mid-way through 2010, by which time the economy is expected to have improved. For the same reason, PWLB rates are expected to increase over time.

3.3 Short Term Rates

The bank base rate remained at 0.5% throughout the quarter.

		April		May		June	
	Start	Mid	End	Mid	End	Mid	End
	%	%	%	%	%	%	%
Call Money (Market)	0.65	0.50	0.50	0.50	0.50	0.45	0.45
1 Month (Market)	1.10	0.90	0.80	0.70	0.65	0.65	0.65
3 Month (Market)	1.70	1.50	1.40	1.35	1.25	1.25	1.25

3.4 Longer Term Rates

		April		May		June	
	Start	Mid	End	Mid	End	Mid	End
	%	%	%	%	%	%	%
1 Year (Market)	2.15	2.15	2.00	2.00	1.95	1.95	1.95
10 Year (PWLB)	3.38	3.38	3.61	3.61	3.87	3.89	3.68
25 Year (PWLB)	4.28	4.39	4.46	4.47	4.68	4.72	4.47

The PWLB rates are for new loans in the "lower quota" entitlements.

3.5 Temporary Borrowing/Investments

Turnover during period

	No. Of Deals Struck	Turnover £m
Short Term Borrowing	2	2.10
Short Term Investments	35	57.20

Position at Month End

	April £m	May £m	June £m
Short Term Borrowing	3.50	3.50	1.50
Short Term Investments	42.45	48.10	44.65

Investment Income Forecast

The forecast income and outturn for the quarter is as follows:

	Cumulative Budget £'000	Cumulative Actual £'000	Cumulative Target Rate %	Cumulative Actual Rate %
Quarter 1	500	578	0.49	5.56
Quarter 2	940			
Quarter 3	1,180			
Quarter 4	1,335			

The investment income return for the first quarter exceeds the target by a considerable margin. This reflects the action taken last year to lock a large proportion of the investment portfolio into longer dated fixed rate investments. However as these deals unwind and current advice and practice is to keep investments of a much shorter duration, the lower replacement rates will see the average rate of return decrease dramatically during the rest of this financial year. Since short term rates are forecast to remain at historic lows for some time the investment income next year will be considerably lower.
The target rate is based on the 7 day libid rate. For comparison purposes the 1 month average rate was 0.65%, 3 month rate 1.25% and 6 months averaging 1.47%.

3.6 Longer Term Borrowing/Investments

The authority did not borrow any new long term money. Due to the economic climate and poor interest rates the authority did not enter into any long term investments.

3.7 Policy Guidelines

Interest Rate Exposure – complied with.

Approved Counterparty List – complied with. During the quarter the authority exceeded the limit with the National Westminster Bank by a small amount over a weekend rather than place the cash with counterparty. The last formal review of the counterparty list was in January 2009, with the next review scheduled for January 2010. However since January there have been numerous downgradings to the credit ratings of many organisations in both the bank and building society sectors, which has changed the exposure limits of organisations within the list. To consolidate the changes and keep members informed of the current position a list of the approved counterparties and their long term rating (as at the 10th July) is attached as an appendix.
Borrowing Instruments – complied with.
Prudential Indicators – complied with:

- Operational Boundary for external debt;
- Upper limit on interest rate exposure on fixed rate debt;
- Upper limit on interest rate exposure on variable rate debt;
- Maturity structure of borrowing as a percentage of fixed rate borrowing;
- Total principal sums invested for periods longer than 364 days;
- Maturity structure of new fixed rate borrowing

4.0 POLICY IMPLICATIONS

4.1 None.

5.0 OTHER IMPLICATIONS

5.1 None.

6.0 IMPLICATIONS FOR THE COUNCIL'S PRIORITIES

6.1 **Children and Young People in Halton**

None.

6.2 **Employment, Learning and Skills in Halton**

None.

6.3 **A Healthy Halton**

None.

6.4 **A Safer Halton**

None.

6.5 **Halton's Urban Renewal**

None.

7.0 RISK ANALYSIS

7.1 The main risks associated with Treasury Management are security of investment and volatility of return. To combat this, the Authority operated within a clearly defined Treasury Management Policy and an annual borrowing and investment strategy, which set out the control framework.

8.0 EQUALITY AND DIVERSITY ISSUES

8.1 There are no issues under this heading.

9.0 LIST OF BACKGROUND PAPERS UNDER SECTION 100D OF THE LOCAL GOVERNMENT ACT 1972

There are no background papers under the meaning of the Act.

Appendix

Last approved EBS 29th January 2009 (as part of quarter3 treasury management report)	Limit <3months >3 months	Ratings as at 10/07/2009 Fitch Long Term Rating	Moody's Long Term Rating
Building Society			
Group A (assets >£10bn)			
Nationwide BS	10/7.5	AA-	Aa3
Britannia BS	10/7.5	A-	A2
Yorkshire BS	10/7.5	A-	Baa1
Group B (assets >£5bn <£10bn)			
Coventry BS	7.5/5	A	A3
Chelsea BS	7.5/5	BBB+	Baa3
Skipton BS	7.5/5	A-	Baa1
Leeds BS	7.5/5	A	A2
West Bromwich BS	7.5/5	BBB-	Baa3
Group C (assets >£1bn <£5bn)			
Principality BS	5/2.5	BBB+	Baa2
Newcastle BS	5/2.5	BBB-	Baa2
Norwich & Peterborough BS	5/2.5	A-	Baa2
Stroud & Swindon BS	5/2.5	N/R	N/R
Nottingham BS	5/2.5	N/R	A3
Progressive BS	5/2.5	N/R	N/R
Cumberland BS	5/2.5	N/R	N/R
Kent Reliance BS	5/2.5	N/R	N/R
National Counties	5/2.5	N/R	N/R
Bank			
(rating AA or better)			
HSBC Plc	10/7.5	AA	Aa2
Banco Santander	10/7.5	AA	Aa1
(rating less than AA)			
Allied Irish Banks Plc (Ireland)	7.5/5	A-	A1
Anglo Irish Banks Plc (Ireland)	7.5/5	A-	A3
Bank of Ireland Plc (Ireland)	7.5/5	A-	A1
Barclays Plc	7.5/5	AA-	Aa3
Cooperative Plc	7.5/5	AA-	A2
Depfa Bank Plc (Ireland)	7.5/5	A-	Aa3
Dexia Bank Plc (Belgium)	7.5/5	A+	A1
LloydsTSB/HBOS Plc	7.5/5	AA-	Aa3
National Westminster Plc (Liq A/c)	7.5/5	AA-	Aa3
Northern Rock Plc	7.5/5	A-	A2
Standard Chartered Bank Plc	7.5/5	A+	A2
Royal Bank of Scotland Plc	7.5/5	AA-	Aa3
Ulster Bank Plc (Ireland)	7.5/5	A+	A2
DMADF (Sovereign Rating)	10/7.5	AAA	AAA