

**AUDIT AND GOVERNANCE COMMITTEE**

**11 February 2011**

**TREASURY MANAGEMENT – THIRD QUARTERLY REVIEW 2010/2011**

**Report of the Executive Director of Commercial and Corporate Services**

**1. Purpose of the Report**

- 1.1. To note the progress in implementing the Treasury Management Borrowing and Investment Strategy for 2010/2011.
- 1.2. This report specifically advises Members of:
  - the progress in implementing the Treasury Management Strategy for 2010/2011 up to the third quarter of the financial year;
  - sets out updates to the authorised institutions that the Council will invest with.

**2. Description of Decision:**

- 2.1 The Committee is recommended to:
  - note the progress made in implementing the borrowing and investment strategy for 2010/2011;
  - note the Council's amended Lending List set out in Appendix 1.

**3 Review of the Prudential Indicators and Treasury Management Strategy for 2010/2011**

- 3.1 The Prudential Indicators for 2010/2011 were approved by the Council on the 3rd March 2010 and are regularly reviewed to ensure that:
  - the Council remains within its Authorised Limit for External Debt;
  - treasury management decisions are taken in accordance with the Treasury Management Code of Practice and existing Council Treasury Management Policy and Strategy Statement;
  - the capital expenditure control framework operated locally is consistent with, and supportive of, local strategic planning, local asset management planning, and proper option appraisal.
- 3.2 Internal monitoring procedures track performance daily against the various prudential indicators agreed by the Council. At this stage, the Council is operating within its Authorised Borrowing Limit, which is a statutory limit determined under Section 3 (1) of the Local Government Act 2003 and there are no areas for concern or any issues which require any review of the indicators as originally approved.

#### 4. Borrowing Strategy for 2010/2011

4.1 The Borrowing Strategy is based upon interest rate forecasts from a number of City institutions. The table below shows the anticipated movement in interest rates since the strategy was approved by Council in March 2010.

	Bank Base Rate		PWLB 5 year Maturity Rate		PWLB 10 year Maturity Rate		PWLB 50 year Maturity Rate	
	March 2010	Dec 2010	March 2010	Dec 2010	March 2010	Dec 2010	March 2010	Dec 2010
March 2011	1.50%	0.50%	3.60%	3.00%	4.45%	4.10%	5.00%	5.20%
March 2012	3.50%	1.00%	4.60%	3.50%	5.00%	4.40%	5.30%	5.50%
March 2013	4.50%	2.25%	4.85%	4.40%	5.15%	5.00%	5.45%	5.60%
March 2014	N/A	3.25%	N/A	5.00%	N/A	5.40%	N/A	5.70%

Economists have been forced to review their economic forecasts in the light of recent events, namely:

- The Sovereign debt crisis that accelerated in May 2010 with Greece and continues to the present time with Ireland and now threatens Portugal and other EU member states.
- The austerity plan introduced by the new coalition government to address the public sector deficit over the next five years.
- The economic growth forecasts for the UK economy which predict weak growth.
- The Bank of England's forecast for inflation - although inflation has remained above the Monetary Policy Committee's (MPC) 2% target, the MPC is confident that inflation will be below the target over the next two years following a further rise to 3.5% by the end of 2010.

Consequently, forecasters are now predicting that the Bank Base Rate and shorter term PWLB rates will remain low for a longer period of time.

4.2 On 20th October 2010, following the Chancellor's announcement of the Spending Review, the Treasury instructed the PWLB to increase the average interest rate on all new loans to an average of 1.00% above the Government's cost of borrowing. This change has resulted in an overall increase in PWLB rates going forward and makes borrowing from this source less affordable.

The Council's strategy for 2010/2011 is to adopt a pragmatic approach and to respond to any changing circumstances to seek to secure benefit for the Council. A benchmark financing rate of 4.50% for long-term borrowing was set for 2010/2011. In response to the Government's increase in PWLB rates across all PWLB loan periods, it is recommended that the Council's benchmark rate for long-term borrowing is increased to 5.50% for the remainder of 2010/2011.

4.3 The Council has borrowed £30.5m in 2010/2011 at an average interest rate of 3.31%, however any further borrowing in 2010/2011 will need to be over shorter term periods to achieve the benchmarking target rate.

4.4 Included in the strategy was provision for debt rescheduling. At this stage, no debt rescheduling has been undertaken in 2010/2011 as rates have not been considered sufficiently favourable.

4.5 The strategy for the remainder of 2010/2011 is to continue to monitor interest rates and to take advantage of any debt rescheduling opportunities that may arise

## **5. Investment Strategy for 2010/2011**

5.1 The primary aim of the Investment Strategy is the security of Council funds, then having regard to liquidity i.e. the availability of cash to meet council liabilities, and finally to secure a reasonable rate of return on its investments.

5.2 As at 31st December 2010, the funds managed by the Council's Treasury Management team has achieved a rate of return on its investments of 1.49% compared with the benchmark rate (i.e. the 7 day rate) of 0.34%. Performance is significantly above the benchmark rate, whilst the treasury management function continues to adhere to the prudent policy agreed by the Council.

The investment policy is monitored to ensure it has flexibility to take full advantage of changes in market conditions.

5.3 The Executive Director of Commercial and Corporate Services, in consultation with the Cabinet Portfolio Holder for Resources, has delegated authority to vary the Lending List Criteria and Lending List itself should circumstances dictate. On 7th October 2010 the Director of Financial Resources, after consultation with Cabinet Portfolio Holder for Resources agreed to add Cater Allen to the Approved Lending List. Although Cater Allen is not individually credit rated it is part of the Santander banking group and it was decided to apply the credit ratings of Santander to Cater Allen as any investments placed with Cater Allen are fully guaranteed by Santander. The addition of Cater Allen to the Approved Lending List gives the Council further flexibility when placing funds and aids the potential for additional yield whilst maintaining proper levels of security and liquidity. The delegated decision is set out at Appendix 1, together with the Approved Lending List (Appendix 2)



<b>RECORD OF DECISION MADE UNDER DELEGATED POWERS</b>	
<b>Department:</b>	Office of the Chief Executive - Financial Resources
<b>Officer making Decision:</b>	Director of Financial Resources
<b>Date of decision:</b>	7/10/2010
<b>Nature of decision made:</b>	
<p>Addition to the Approved Lending List: To add Cater Allen, part of the Santander Banking Group, to the Council's approved Lending List.</p>	
<b>Reason for decision:</b>	
<p>Where an organisation (which is not individually credit rated) is part of a group, and is wholly guaranteed by that group, then the credit ratings of that group can be applied to the organisation to determine its credit limit and rating.</p> <p>Therefore, Cater Allen, being part of the Santander Banking Group means that although it is not individually "credit rated" it can assume the rating of the Santander Banking Group. All deposits placed with Cater Allen are fully and unconditionally guaranteed by Santander UK Plc., which is a highly rated financial institution and is also included in the Government's Credit Guarantee Scheme.</p> <p>The Council has a copy of the letter of guarantee by Santander and this has been reviewed by our legal section as being in order and they have confirmed that this provides the Council with the appropriate assurance to include Cater Allen on the Council's Lending List.</p> <p>The group limit for Santander will not change from the current level of £40 million but any deposits made with Cater Allen will count against the Group Limit for the Santander Banking Group. The decision will mean that the Council can then deal with Cater Allen as appropriate.</p>	
<b>Members/Officers consulted (attach their views as appropriate)</b>	Cllr D. Allan
<b>File/background papers used:</b>	Letter of Guarantee by Santander and Legal Advice
<b>Is this a confidential matter as referred to in paragraph 7 of the Guidance?</b>	No
<b>Paragraph of Delegation Scheme relied upon:</b>	Council approved on 4 <sup>th</sup> March 2009 that "delegated authority be given to the City Treasurer, (now Director of Financial Resources), in consultation with the Cabinet Portfolio holder for Resources, to vary the Lending List Criteria and the

Lending List should circumstances dictate, on the basis that changes be reported to Cabinet retrospectively”.

**Signature:**.....

**Date:** 7<sup>th</sup> October 2010

**Counter Signature:**.....

**Date:**

Approved Lending List

Appendix 2

	Fitch				Moody's			Standard & Poor's		Limit £m	Max Deposit Period
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength	L Term	S Term		
<b>UK</b>	AAA	F1+			Aaa			AAA		300	364 days
<b>Lloyds Banking Group</b> (see Note 1)										<b>Group Limit 50</b>	
Lloyds Banking Group plc	AA-	F1+	C	1	Aa3	-	-	A	A-1	50	364 days
Lloyds TSB Bank Plc	AA-	F1+	C	1	Aa3	P-1	C-	A+	A-1	50	364 days
Bank of Scotland Plc	AA-	F1+	C	1	Aa3	P-1	D+	A+	A-1	50	364 days
<b>Royal Bank of Scotland Group</b> (See Note 1)										<b>Group Limit 50</b>	
Royal Bank of Scotland Group plc	AA-	F1+	C/D	1	A1	P-1	-	A	A-1	50	364 days
The Royal Bank of Scotland Plc	AA-	F1+	C/D	1	Aa3	P-1	C-	A+	A-1	50	364 days
National Westminster Bank Plc	AA-	F1+	-	1	Aa3	P-1	C-	A+	A-1	50	364 days
Ulster Bank Ltd	A+	F1+	E	1	A2	P-1	D-	A	A-1	50	364 days
<b>Santander Group *</b>										<b>Group Limit 40</b>	
Santander UK plc	AA-	F1+	B	1	Aa3	P-1	C-	AA	A-1+	40	364 days
Cater Allen	AA-	F1+	B	1	Aa3	P-1	C-	AA	A-1+	40	364 days
Barclays Bank plc *	AA-	F1+	B	1	Aa3	P-1	C	AA-	A-1+	40	364 days
HSBC Bank plc *	AA	F1+	B	1	Aa2	P-1	C+	AA	A-1+	40	364 days

**Appendix 2(continued)**

	Fitch			Support	Moody's			Standard & Poor's		Limit £m	Max Deposit Period
	L Term	S Term	Individual		L Term	S Term	Fin Strength	L Term	S Term		
Nationwide BS *	AA-	F1+	B	1	Aa3	P-1	C-	A+	A-1	40	364 days
Standard Chartered Bank *	AA-	F1+	B	1	A2	P-1	C+	A+	A-1	40	364 days
Clydesdale Bank / Yorkshire Bank **	AA-	F1+	C	1	A1	P-1	C-	A+	A-1	10	364 days
Co-Operative Bank Plc	A-	F2	B/C	3	A2	P-1	D+	-	-	5	6 months
Northern Rock ***	BBB+	F2	C	2	-	-	-	A-	A-2	0	
<b>Top 10 Building Societies (by asset value)</b>											
Nationwide BS (see above)											
Yorkshire BS	A-	F2	B/C	5	Baa1	P-2	D+	A-	A-2	0	
Coventry BS	A	F1	B	5	A3	P-2	C-	-	-	5	6 Months
Skipton BS	A-	F2	B/C	5	Baa1	P-2	D+	-	-	0	
Leeds BS	A	F1	B/C	5	A2	P-1	C+	-	-	10	364 Days
West Bromwich BS ***	BBB-	F3	C/D	5	Baa3	P-3	E+	-	-	0	
Principality BS ***	BBB+	F2	C	5	Baa2	P-2	D-	-	-	0	
Newcastle BS ***	BBB-	F3	C/D	5	Baa2	P-2	D-	-	-	0	
Norwich and Peterborough BS ***	BBB+	F2	C	5	Baa2	P-2	D	-	-	0	
Nottingham BS	-	-	-	-	A3	P-2	C-	-	-	5	6 Months
<b>Foreign Banks have a combined total limit of £40m</b>											
<b>Australia</b>	AA+	-	-	-	Aaa	-	-	AAA		40	364 Days
National Australia Bank	AA	F1+	B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
Australia and New Zealand Banking Group Ltd	AA-	F1+	B	1	Aa1	P-1	B	AA	A-1+	20	364 Days



<b>Appendix 2 (continued)</b>											
	<b>Fitch</b>				<b>Moody's</b>			<b>Standard &amp; Poor's</b>			
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength	L Term	S Term	Limit £m	Max Deposit Period
Commonwealth Bank of Australia	AA	F1+	A/B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
Westpac Banking Corporation	AA	F1+	A/B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
<b>Canada</b>	<b>AAA</b>				<b>Aaa</b>			<b>AAA</b>		40	364 Days
Bank of Nova Scotia	AA-	F1+	B	1	Aa1	P-1	B	AA-	A-1+	20	364 Days
Royal Bank of Canada	AA	F1+	A/B	1	Aa1	P-1	B+	AA-	A-1+	20	364 Days
Toronto Dominion Bank	AA-	F1+	B	1	Aaa	P-1	B+	AA-	A-1+	20	364 Days
<b>Money Market Funds</b>										50	2 Years
Prime Rate Stirling Liquidity	AAA MMF							AAAm		30	2 Years
Insight Liquidity Fund					AAA MR1			AAAm		30	2 Years
Ignis Sterling Liquidity	AAA MMF							AAAm		30	2 Years

## Notes

### Note 1 Nationalised / Part Nationalised

The counterparties in this section will have the UK Government's AAA rating applied to them thus giving them a revised credit limit of £50 million for a maximum period of 364 days

\* Banks / Building Societies which are part of the UK Government's Credit Guarantee scheme  
The counterparties in this section will have an AA rating applied to them thus giving them a revised credit limit of £40 million for a maximum period of 364 days

\*\* The Clydesdale Bank (under the UK section) is owned by National Australia Bank

\*\*\* These will be revisited and used only if they meet the minimum criteria (ratings of A- and above)

Any bank which is incorporated in the United Kingdom and controlled by the FSA is classed as a UK bank for the purposes of the Approved Lending List.

