CYNGOR SIR *POWYS* COUNTY COUNCIL.

STRATEGIC BOARD
1st September 2010

REPORT AUTHOR: **County Councillor Tony Thomas**
Portfolio Holder for Finance

SUBJECT: **Treasury Management Quarterly Report**

REPORT FOR: **Information**

Summary

1. Introduction

1.1 The Treasury Management Scrutiny Review recommended that quarterly reports to Board should be adopted. CIPFA also issued a Treasury Management Bulletin March 2009 highlighting interim advice to local authorities on treasury management practices in the light of the Icelandic Banks collapse and the continuing "credit crunch". The document suggested:

"In order to enshrine best practice it is suggested that authorities report formally on treasury management activities at least twice a year and preferably quarterly."

1.2 This report, therefore, is providing information on the activities for the quarter ending 30th June 2010.

2. Economic Background and Forecasts

2.1 The economic background is attached at Appendix A.

2.2 The most recent forecast of interest rates by the Authority's advisor is:

	Sep 10	**Dec 10**	**Mar 11**	**Jun 11**	**Sep 11**	**Dec 11**	**Mar 12**	**Jun 12**
Bank rate	0.50%	0.50%	0.75%	0.75%	1.00%	1.50%	2.00%	2.25%
5yr PWLB	2.50%	2.60%	2.80%	2.95%	3.20%	3.45%	3.80%	4.15%
10yr PWLB	3.80%	3.85%	4.00%	4.20%	4.40%	4.50%	4.70%	4.75%
25yr PWLB	4.45%	4.50%	4.55%	4.70%	4.80%	4.90%	5.05%	5.15%
50yr PWLB	4.45%	4.55%	4.60%	4.75%	4.85%	4.95%	5.05%	5.25%

The forecast has been revised as there are concerns that the acceleration of the elimination of the budget deficit will have a dampening effect on economic growth and will leave less room for the MPC to raise Bank Rate as fast and as far as previously expected.

There are also considerable risks around a re-emergence of major sovereign debt concerns in the EU during 2010 which could increase the safe haven status of UK gilts and put further downward pressure on gilt yields during 2010/11.

Other concerns such as the durability of the coalition government, acceptance of job cuts and pension cuts without stimulating strikes, the lack of growth in other countries undermining the potential for growth in UK exports and therefore, overall UK growth, could also put downward pressure on yields.

However, the advisors maintain that the general trend beyond 2010 of rising gilt yields is expected to remain unchanged as market fundamentals must eventually re-establish the current disconnect between the sheer volume of UK gilt issuance and the price of issue of new debt.

3. Treasury Management Strategy

3.1 Board on 9th February and 30th March 2010 and Full Council on 29th April 2010 approved the Investment Strategy for 2010/11 as follows:

Long Term Ratings:

Permitted Fitch Ratings	Permitted Moodys Ratings	Permitted S&P Ratings
AAA	Aaa	AAA
AA+	Aa1	AA+
AA	Aa2	AA
AA-	Aa3	AA-

Short Term Ratings:

Permitted Fitch Ratings	Permitted Moodys Ratings	Permitted S&P Ratings
F1+	N/A	A-1+
F1	P-1	A-1

Country Limits:

Country	**Maximum Investment per Country**	**Credit Rating/Other Assessment of Risk**
AAA rated – countries (excluding the UK) listed at Appendix C	£2M	As per rating list
AAA rated – UK	No Maximum Investment	As per rating list

Group/Institutions - Counterparty Criteria/Limits:

Specified Investments:

Institution	**Maximum Investment per Group/ Institution £M**	**Maximum Length**	**Credit Rating/Other Assessment of Risk**
UK Banks	10	Up to 364 days	As per Sector's matrices and the Authority's definition of a high credit rating
Foreign Banks	2	Up to 364 days	As per Sector's matrices and the Authority's definition of a high credit rating
Other Local Authorities	25 (2M limit with any one authority)	Up to 364 days	N/A

Non-Specified Investments:

Institution	**Maximum Investment per Group/Institution £M**	**Maximum Length**	**Credit Rating/Other Assessment of Risk**
UK Banks	10 (No more than £3m long term with any one institution in respect of new investments)	Up to 2 years	As per Sector's matrices and the Authority's definition of a high credit rating
Foreign Banks	2	Up to 2 years	As per Sector's matrices and the Authority's definition of a high credit rating
Money Market Funds (maximum of 3)	10	N/A	All are AAA rated
Other Local Authorities	10 (2M limit with any one authority)	Up to 2 years	N/A
European Investment Bank Bonds	3	2-3 years	N/A

Note: Limits for Specified and Non-Specified are combined limits. The maximum limit will also apply to a banking group as a whole e.g. Lloyds TSB and BOS will have an overall limit of £10M.

4. Current Investments

4.1 The Authority's investment position as at 30th June 2010 is as shown below:-

Borrower	**Principal £**	**Interest Rate**	**Current Limits**	**Maturity Date**
Bank of Scotland	4,000,000	0.75%	10,000,000	Deposit A/c
HSBC	1,000,000	0.45%	10,000,000	Deposit A/c
Royal Bank of Scot	5,000,000	0.86%	10,000,000	Deposit A/c
Barclays Global	10,000,000	0.41%	10,000,000	MMF
Standard Life	10,000,000	0.43%	10,000,000	MMF
Royal Bank of Scot	5,000,000	0.95%	See above	19.08.2011
Lloyds TSB	3,000,000	1.08%	See BOS above	22.09.2010
Lloyds TSB	3,000,000	1.48%	See BOS above	22.02.2011
Barclays	5,000,000	0.95%	10,000,000	03.12.2010
Barclays	5,000,000	0.94%	See Barclays above	13.12.2010
Total Investments	**51,000,000**			

The table above excludes investments still held in Iceland.

4.2 Due to the downgrading of Spain's sovereign rating on 1st June 2010, it was felt appropriate to withdraw the £10M deposit from the deposit account with Santander UK. The Authority continues to hold weekly amounts of up to £30k with Santander in respect of establishments who use Post Offices to bank income.

4.3 All European banks have subsequently undergone stress testing which was co-ordinated by the Committee of European Banking Supervisors. Banco Santander was the highest ranking bank in this testing.

5. Redemption Penalties

5.1 Royal Bank of Scotland have indicated that they would consider early redemption of investments if required but they have not provided a cost at this time.
The Lloyds TSB and Barclays investments are not available for early redemption.

6. Market rates

6.1 Current market rates available for fixed term deposits are attached at Appendix B for information.

7. Credit Rating Changes

7.1 The credit rating list for end of June is attached as a separate file to this report.

7.2 UK Sovereign Rating:

Following the announcement of the UK emergency budget on 22nd June 2010, all three major credit rating agencies have given their view on the possible effects on the UK AAA Sovereign rating.

Fitch and Moody's were supportive in their view with Moody's saying that the UK budget is supportive of the country's Aaa rating and stable outlook because it is a key step towards reversing the significant deterioration in the government's financial position that occurred over the past two years. The budget was also broadly in line with expectations, both in terms of the mix of spending cuts and tax increases, and in its more downbeat economic growth projections.

Moody's also noted that the government's plan incorporates conservative economic growth forecasts and that, lower trend GDP growth, if it occurred, would likely be reflected in equally lower growth in current expenditures over time.

Fitch said that the Budget statement was a strong statement of intent by the new UK government to accelerate the path of deficit reduction and stabilise and reduce the public debt burden. Fitch's preliminary assessment of the budget was that it set out an ambitious deficit reduction path that, if delivered upon, would materially strengthen confidence in UK public finances and the UK's AAA status.

Standard & Poors however, said that it was too early to assess the impact of Britain's budget on the nation's AAA status.

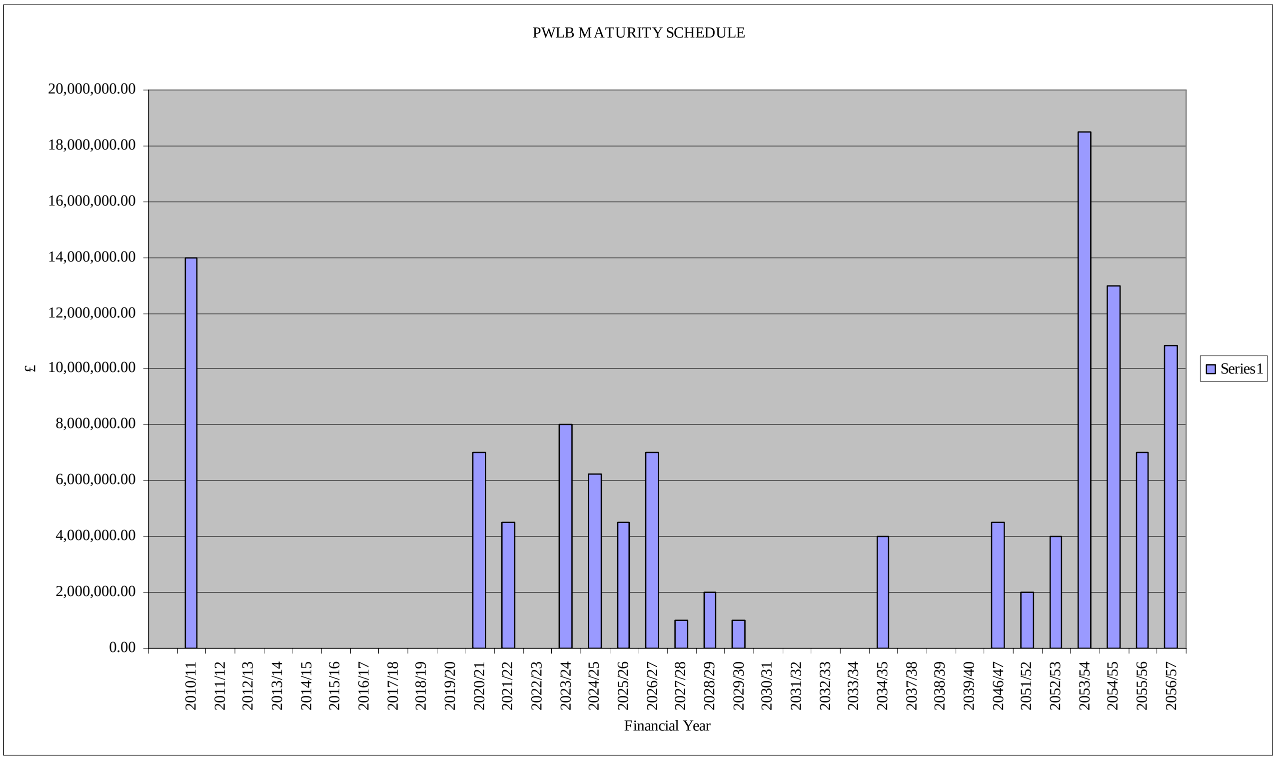
For information, Fitch and Moody's AAA ratings are on stable outlook whilst Standard & Poors have maintained a negative outlook on the rating.

8. <u>Borrowing / Re-scheduling</u>

8.1 Effective management of the Authority's debt is essential to ensure that the impact of interest payable is minimised against our revenue accounts whilst maintaining prudent borrowing policies.

8.2 *Debt Maturity Profile as at 30.06.10:*

(please click on the graph below and increase the percentage in the toolbar above for an enhanced view)



8.3 With effect from 26th April 2010, the Public Works Loans Board introduced two regular intra-daily re-sets of rates published at 9.30 a.m. and 12.30 p.m. It had been anticipated that this introduction of intra-day rates may provide local authorities with more favourable options to repay debt. However, at present, this has not been the case with rates not having been conducive towards premature repayments of debt.

8.4 Board are aware that officers continue to look for interest savings on a daily basis.

9. Prudential Indicators

9.1 All Prudential Indicators were complied with in the quarter ending 30th June 2010.

Proposal

It is proposed that Board receives the Treasury Management Quarterly Report.

Corporate Improvement Plan

Not applicable.

Options Considered/Available

Not applicable

Preferred Choice and Reasons

Not applicable

Sustainability and Environmental Issues/Equalities/Crime and Disorder,/Welsh Language/Other Policies etc

Not applicable

Local Member(s)

Not applicable

Other Front Line Services

Not applicable

Support Services (Legal, Finance, HR, ICT, BPU)

Local Service Board/Partnerships/Stakeholders etc

Not applicable

Communications

Statutory Officers

Not applicable

Future Status of the Report

Not applicable

Recommendation:	Reason for Recommendation:
That Board receives the Treasury Management Quarterly Report	

Relevant Policy (ies):	Treasury Management Policy		
Within Policy:	Y	Within Budget:	Y

Relevant Local Member(s):	

Person(s) To Implement Decision:	Ann Owen – Treasury Manager
Date By When Decision To Be Implemented:	

Contact Officer Name:	Tel:	Fax:	Email:
Ann Owen	01597 826327	01597 826290	ann.owen@powys.gov.uk

Background Papers used to prepare Report:

CIPFA Code of Practice on Treasury Management and Cross Sectoral Guidance Notes

Treasury Management Policy Statement

Advisors' Information

WAG Guidance on Local Government Investments 2010

Appendix A:

ECONOMIC BACKGROUND

The UK was in an uncomfortable position as it faced a budget deficit of over 12% of its GDP and the new coalition government in May outlined £6.25bn of immediate spending cuts. This was followed by the Government's first budget which set out a 5 year plan to reduce the deficit, rebalance the economy and design a new model for economic growth. The bulk of debt reduction will come from lower spending (77%) rather than higher taxes (23%).

The Bank of England left the bank rate at the record low of 0.5% in April, May and June although one member voted for an increase in June. It also explained it would keep its asset buying programme unchanged at £200 billion although one member thought that June was the right time to withdraw this given the continued above target rate of inflation.

The CPI inflation figure fell to 3.4% from 3.7% while the RPI figure saw inflation at its highest rate in 19 years at 5.4%. The number of people unemployed was 2.47M over the quarter, an increase of 23,000.

The volume of sales on the high street fell in the quarter compared with a year ago. The resulting balance of -5 was better than had been predicted (-15).

The property market continued to show signs of slowing down. Halifax reported that property prices had fallen. However this was in contrast to the Nationwide who reported that prices had risen slightly.

After an initially muted reaction towards the release of the UK budget statement the Pound rocketed, ending the quarter at $1.496. The Euro had a poor month in June losing ground against the Pound ending at E1.223 having started the month at E1.198.

Appendix B:

MARKET RATES AVAILABLE

Banks:

Duration	**%**
Overnight	0.45 – 0.50
1 Week	0.45 – 0.55
2 Week	0.45 – 0.55
1 Month	0.50 – 0.70
2 Month	0.55 – 0.75
3 Month	0.65 – 0.85
4 Month	0.75 – 0.95
5 Month	0.85 – 1.05
6 Month	0.95 – 1.15
9 Month	1.20 – 1.40
10 Month	1.25 – 1.45
11 Month	1.35 – 1.55
12 Month	1.40 – 1.60

Building Societies:

Duration	**%**
1 Month	0.55
2 Month	0.70
3 Month	0.90
4 Month	1.00
5 Month	1.10
6 Month	1.25
9 Month	1.45
10 Month	1.50
11 Month	1.50
12 Month	1.65