APPENDIX

ANNUAL TREASURY REPORT 2011/12

1. Introduction and Background

The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2009 was adopted by this Council on 24 February 2010.

The primary requirements of the Code are as follows:

(1) Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
(2) Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
(3) Receipt by the Full Council of an annual treasury management strategy report (including the annual investment strategy*)* for the year ahead and an annual review report of the previous year.
(4) Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
(5) Delegation by the Council of the role of scrutiny of the treasury management strategy to a specific named body which in this Council is the Transformation and Resources Overview and Scrutiny Committee.
(6) Delegation by the Council of the role of scrutiny of treasury management performance to a specific named body which in this Council is the Audit and Risk Committee, a midyear review report is received by this Committee.

Treasury management in this context is defined as:

"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks. "

The purpose of this report is to meet one of the above requirements of the CIPFA Code, namely the annual review report of treasury management activities, for the financial year 2011/12.

2. This Annual Treasury Report Covers

- The Council's treasury position as at 31 March 2012;
- The strategy for 2011/12;
- The economy in 2011/12;
- Investment rates in 2011/12;
- Compliance with treasury limits and Prudential Indicators;
- Investment outturn for 2011/12;
- Involvement of Elected Members;
- Other issues.

3. Treasury Position as at 31 March 2012

The Council's investment position at the beginning and the end of the year was as follows:

	At 31/3/12	Return	Average Life (Days)	At 31/3/11	Return	Average Life (Days)
Total Debt	*£0m*	*N/A*	*N/A*	*£0m*	*N/A*	*N/A*
Total Investments	*£10.475m*	*1.03%*	*22*	*£17.700m*	*1.13%*	*181*

The decline in total investments has been due to a combination of few capital receipts being received due to the economic downturn and capital expenditure being incurred, chiefly on Jubilee 2.

4. The Strategy for 2011/12

The strategy agreed by Council on 23 February 2011 was that:

- There would be no long term borrowing for capital purposes;
- Short term borrowing would be required to cover any temporary shortfalls in revenue income and to temporarily fund capital expenditure during the interim period before a permanent means of finance became available;
- All borrowing would be kept absolutely within the Authorised Limit of £15m and would not normally exceed the Operational Boundary of £5m (although it could for short periods of time be permitted to rise to a figure between £5m and £15m due to variations in cash flow);
- Temporary surpluses which might arise would be invested, either in short term deposits with the Council's bankers or in money market investments (cash deposits) if the size warranted this and for an appropriate period in order that these sums would be available for use when required;
- The proportions of loans and investments to be at fixed or variable rates were: fixed rate loans to be between 0% and 100% of the total and fixed rate investments to be between 0% and 100% of the total;
- Long term investments to be permitted as follows: maturing beyond 31/03/11 £10m, maturing beyond 31/03/12 £10m, maturing beyond 31/03/13, £10m;
- The overriding consideration in determining where to place the Council's surplus funds was to safeguard the Council's capital. Within this constraint the aim was to maximise the return on capital; and,
- Forward commitment of funds for investment is permitted in respect of in house investments.

Changes in strategy and credit Policy during the year

There have been no changes to the Treasury Management Strategy during the year. As approved by Council on 30 July 2008 we continue to use the lowest common denominator methodology in respect of determining suitable counterparties. This methodology is based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc.).

This, and the downgrading of numerous Banks and Building Societies, has led to a severely restricted counterparty listing remaining, resulting in a limited number of counterparties with whom the Council can invest with.

5. The Economy and Interest Rates

The financial year 2011/12 continued the challenging investment environment of previous years, namely low investment returns and continuing heightened levels of counterparty risk. The original expectation for 2011-12 was that the Bank Rate would start gently rising from quarter 4 2011. However, GDP growth in the UK was disappointing during the year under the weight of the UK austerity programme, a lack of rebalancing of the UK economy to exporting and weak growth in our biggest export market - the EU. The EU sovereign debt crisis grew in intensity during the year until February when a second bailout package was eventually agreed for Greece. Weak UK growth resulted in the Monetary Policy Committee increasing quantitative easing by £75bn in October and another £50bn in February. The Bank Rate therefore ended the year unchanged at 0.5% while CPI inflation peaked in September at 5.2% but then fell to 3.4% in February, with further falls expected to below 2% over the next two years.

Gilt yields fell for much of the year, until February, as concerns continued building over the EU debt crisis. This resulted in safe haven flows into UK gilts which, together with the two UK packages of quantitative easing during the year, combined to depress PWLB rates to historically low levels.

6. Investment Rates in 2011/12

Widespread and multiple downgrades of the ratings of many banks and countries, continued Eurozone concerns and the significant funding issues still faced by many financial institutions meant that investments remained short term. This led to the banks offering instant deposit accounts at more preferential rates than short term fixed deposits in most cases. The Council opted to take advantage of these accounts and this is reflected in the significantly reduced average life (days) of its deposits.

7. Compliance With Treasury Limits

During the financial year the Council operated within the treasury limits and Prudential Indicators set out in the Council's annual Treasury Strategy Statement. The outturn for the Prudential Indicators is shown in Annex 1.

8. Investment Outturn For 2011/12

Internally Managed Investments

The Council manages its investments in-house and invests with the institutions listed in the Council's approved lending list. The Council invested for a range of periods from overnight to up to 4 months dependent on the Council's cash flows, its interest rate view and the interest rates on offer. The investments made in 2011/12 in practice were generally for a period of less than 3 months.

Investment Outturn for 2011/12

During 2011/12 an average rate of return of 1.03% was achieved on an average individual investment of £1.074m. This compared with the target of 1% included in the departmental business plan.

9. Involvement of Elected Members

Elected members have been involved in the treasury management process during 2011/12 including:

- Scrutiny of the treasury management strategy by the Transformation and Resources

Overview and Scrutiny Committee prior to being submitted for approval by the Full Council.
- Scrutiny of treasury management performance by the Audit and Risk Committee through the receipt of a half yearly treasury management report.
- Quarterly liaison meetings took place, to be attended by the Council's Treasury Management advisors, Sector and the Portfolio Holder for Resources and Efficiency.
- The Portfolio Holder for Resources and Efficiency sent a monthly budget monitoring report which contains details of Treasury Management activity undertaken during the month; and this was forwarded to all Members.
- A quarterly budget monitoring and performance report is reported to Cabinet, this contains details of Treasury Management activity undertaken during the quarter.

10. Icelandic Bank Defaults

This authority currently has the following investment frozen in the Heritable Bank:

- Investment 5092, £2.5m, maturity date 14th September 2009.

Payments up to 31 March 2012 totalled £1,225,905. Two further payments have been received, £95,089 on 19 April 2012, and £71,528 on 19 July 2012**.**

Annex 1: Prudential Indicators

	Position/Prudential Indicator	2010/11 Actual	2011/12 Original Indicator	2011/12 Actual
1	Capital Expenditure	£9.682m	N/A	£14.796m
2	Capital Financing Requirement at 31 March 2012	£0.115m	£0.115m	£(0.031m)
3	Treasury Position at 31 March 2011			
	Borrowing	£0.0m	N/A	£0.0m
	Other long term liabilities	£0.0m	N/A	£0.0m
	Total Debt	(£0.0m)	N/A	(£0.0m)
	Investments	(£17.700m)	N/A	(£10.475m)
	Net Borrowing	(£17.700m)	N/A	(£10.475m)
4	Authorised Limit (against maximum position)	£0.0m	£15.0m	£0.0m
5	Operational Boundary (against maximum position)	£0.0m	£5.0m	£0.0m
6	Ratio of Financing Costs to Net Revenue Stream	(1.80%)	(0.56%)	(1.23%)
7	Upper Limits on Variable Interest Rates (against maximum position)			
	Loans	0%	100%	0%
	Investments	0%	100%	0%
8	Actual External Debt	£0.0m	N/A	£0.0m
9	Principal Funds Invested for Periods Longer than 364 days (against maximum position)	£0.0m	£10.0m	£0.0m

GLOSSARY

CPI – Consumer Price Index
The Consumer Price Index (CPI) is the main UK measure of inflation for macroeconomic purposes and forms the basis for the Government's inflation target. It is also used for international comparisons.

LIBID – London Interbank Bid Rate
Banks in the City of London tend to lend and borrow money from one another in the wholesale money markets. The rate at which a bank is willing to borrow money is called the London Interbank Bid Rate (LIBID).

LIBOR – London Interbank Offered Rate
This is the benchmark used by banks, securities houses and investors to gauge the cost of unsecured borrowing in the money markets. It is calculated each day by asking a panel of major banks what it would cost them to borrow funds for various periods of time and in various currencies, and then creating an average of the individual bank's figures.

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MPC – Monetary Policy Committee
Interest rates are set by the Bank's Monetary Policy Committee (MPC). The MPC sets an interest rate it judges will enable the inflation target to be met. The Bank's MPC is made up of nine members – the Governor, the two Deputy Governors, the Bank's Chief Economist, the Executive Director for Markets and four external members appointed directly by the Chancellor. The appointment of external members is designed to ensure that the MPC benefits from thinking and expertise in addition to that gained inside the Bank of England.

PWLB – Public Works Loan Board
The Public Works Loan Board (PWLB) is a statutory body operating within the Debt Management Office and is responsible for lending money to local authorities and other prescribed bodies, as well as for collecting the repayments.