Item 9

Corporate Services Overview and Scrutiny Committee

16th October 2013

Treasury Management Outturn Report 2012/13

Recommendation

That the Corporate Services Overview and Scrutiny Committee considers and comments on the annual Treasury Management outturn report in respect of 2012/13.

1 Introduction

1.1 Warwickshire County Council fully complies with the requirements of The Chartered Institute of Public Finance and Accountancy's (CIPFA's) Code of Practice (COP) on Treasury Management 2009. The primary requirements of the Code are the:

- creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities;
- creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives;
- receipt by the Cabinet of an annual treasury management strategy report for the year ahead, a midyear review report (as a minimum) and an annual review report of the previous year;
- 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.

1.2 Therefore, under the CIPFA Code, the Authority is required to receive a report on the outturn of the annual treasury management activity.

1.3 Treasury management in the context of this report is defined as:

"The management of the local authority's 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." *(CIPFA Code of Practice)*.

1.4 This annual treasury outturn report covers:

- Council’s Current Treasury Position — Section 2
- Performance Measurement — Section 3
- Treasury Management Strategy for 2012/13 — Section 4
- The Economy and Investment Rates in 2012/13 — Section 5
- Borrowing Outturn for 2012/13 — Section 6
- Compliance with Treasury Limits and Prudential Indicators — Section 7
- Investment Rates 2012/13 — Section 8
- Investment Outturn 2012/13 — Section 9
- Debt Rescheduling for 2012/13 — Section10

2 Council’s Current Treasury Position

2.1 The Council raises long-term borrowing to fund capital expenditure, i.e., expenditure on land, buildings and equipment. The Council did not take any borrowing in 2012/13, there was £391.6m of long-term borrowing as at 31 March 2013.

2.2 At the same time as borrowing for capital purposes, the Council also has an investment portfolio. This consists of the Council’s reserves and short-term cash flows. This cash was invested partly by an external cash manager and partly in house. As at 31 March 2012, the Council had £209.3 of cash investments and this had increased to £221.4m by 31 March 2013 as detailed in section B of Table 1.

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

Table 1: Summary of Treasury Position at 31 March 2013

	Principal at 31.03.12	**Rate/ Return**	**Principal at 31.03.13**	**Rate/ Return for 12/13**
A: Fixed Rate Funding	£m	%	£m	%
Public Works Loans Board Debt	391.6	4.95	391.6	4.95
Total Debt	**391.6**	**4.95**	**391.6**	**4.95**
B: Investments				
In House	163.0	0.45	174.4	0.39
External Managers	46.3	1.40	47.0	1.56
Total Investments	**209.3**	**0.66**	**221.4**	**0.98**

3 Performance Measurement

3.1 One of the key changes in the last revision of the CIPFA Code was the formal introduction of performance measurement relating to investments, debt and capital financing activities. Whilst investment performance criteria have been well developed and accepted, debt performance indicators continue to be a more problematic area with the traditional average portfolio rate of interest acting as the main guide (as incorporated in Table 1).

4 Treasury Management Strategy for 2012/13

4.1 Our treasury strategy for 2012/13 was approved by Cabinet on 16 February 2012 and then Council on 27 March 2012.

4.2 The expectation for interest rates within the strategy for 2012/13 anticipated low but rising Bank Rate (starting in quarter 4 of 2014) with similar gradual rises in medium and longer term fixed borrowing rates over 2012/13. Variable or short-term rates were expected to be the cheaper form of borrowing over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

4.3 The actual movement in gilt yields meant that PWLB rates fell during the first quarter of the year to historically low levels. This was caused by a flight to quality into UK gilts from EU sovereign debt, and from shares, as investors became concerned about the potential for a Lehman's type crisis of financial markets if the Greek debt crisis were to develop into a precipitous default and exit from the Euro. During the second and third quarters, rates rose gradually and agreement of a second bail out for Greece in December saw the flight to quality into gilts reverse somewhat, as confidence rose that the Eurozone crisis was finally subsiding. However, gilt yields then fell back again during February and March as Eurozone concerns returned, with the focus now shifting to Cyprus, and flight to quality flows into gilts resumed. This was a volatile year for PWLB rates, driven by events in the Eurozone which oscillated between crises and remedies.

5 The Economy and Investment Rates in 2012/13

5.1 The financial year 2012/13 continued the challenging investment environment of previous years, namely low investment returns and continuing heightened levels of counterparty risk. The original expectation for 2012/13 was that Bank Rate would start gently rising from quarter 4 2014. However, economic growth in the UK was disappointing during the year due to the UK austerity programme, weak consumer confidence and spending, a lack of rebalancing of the UK economy to exporting and weak growth in our biggest export market - the European Union (EU).

5.2 The UK coalition Government maintained its tight fiscal policy stance against a background of warnings from two credit rating agencies that the UK could lose its AAA credit rating. Moody's followed up this warning by actually downgrading the rating to AA+ in February 2013 and Fitch then placed their rating on negative watch, after the Budget statement in March. Key to retaining the AAA rating from Fitch and S&P will be a return to strong economic growth in order to reduce the national debt burden to a sustainable level, within a reasonable timeframe.

5.3 Weak UK growth resulted in the Monetary Policy Committee increasing quantitative easing by £50bn in July to a total of £375bn. Bank Rate therefore ended the year unchanged at 0.5% while CPI inflation fell from 3% at the start of the year to end at 2.8% in March, with a fall back to below 2% pushed back to quarter 1 2016. The EU sovereign debt crisis was an ongoing saga during the year with first Greece and then Cyprus experiencing crises which were met with bailouts after difficult and fraught negotiations.

6 Borrowing Outturn for 2012/13

6.1 The Council did not take any PWLB borrowing in 2012/13.

7 Compliance with Treasury Limits and Prudential Indicators

7.1 During the financial year the Council operated within the treasury limits and Prudential Indicators set out in the Council's Treasury Policy Statement and Treasury Management Strategy.

7.2 Table 2 compares actual performance against the 2012/13 borrowing limits and shows that all treasury activity was conducted within the set limits.

Table 2: Actuals Compared with Strategy Limits 2012/13

	Limit	**Actual**
Authorised Limit for External Debt	£592.7m	£391.6
Upper Limit for Interest Rate Exposure	100%	100%
Upper Limit for Variable Rate Exposure	25%	0%
Upper Limit for total principal sums invested for over 365 days	£0	£0
Maturity Structure of Fixed Rate borrowed during 2012/13		
Under 12 months	0-20%	0%
12 months and within 24 months	0-20%	0%
24 months and within 5 years	0-60%	0%
5 years and within 10 years	0-100%	0%
10 years and above	0-100%	0%

7.3 Full details of the Prudential indicators set for 2012/13 and the results for the year are shown in **Appendix A.**

8 Investment Rates 2012/13

8.1 The Bank Rate remained at its historic low of 0.50% throughout the year; it has now remained unchanged for four years. Market expectations of the start of monetary tightening were pushed back during the year to early 2015 at the earliest. The Funding for Lending Scheme resulted in a sharp fall in deposit rates in the second half of the year.

9 Investment Outturn for 2012/13

9.1 The Council's investment policy is governed by CLG guidance, which was been implemented in the annual investment strategy approved by the Council on 27 March 2013. This policy sets out the approach for choosing investment counterparties, and 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).

9.2 The Council manages its short-term cash balances in-house and invests with the institutions listed in the Council's approved lending list. The Council invests for a range of periods from overnight to one year, dependent on the Council's cash flows, its interest rate view and the interest rates on offer. Table 3 summarises the investment performance for 2012/13.

Table 3: Investment Outturn 2012/13

	Average balance of Investments £m	**Rate of Return %**	**Benchmark Return %**
Internally Managed	190.5	0.39	0.39
Externally Managed	46.8	1.45	0.43

9.3 Reserves and long-term cash balances are placed with an external cash manager, Aviva Investors, who invests in a wide range of investment instruments. The fund management agreement between the Council and the Fund Manager defines the limits for maximum weighting in gilts/bonds and maximum duration of the fund. Counterparty criteria and exposure limits are also pre-defined within the agreement.

9.4 Aviva's performance target was to out-perform the 7-day investment rate by 10% of the benchmark rate. During 2012/13, Aviva achieved a return of 1.45%. This is substantially above its target of 0.43%

9.5 No institutions in which investments were made had any difficulty in repaying investments and interest in full during the year.

10 Debt Rescheduling for 2012/13

10.1 No debt rescheduling was undertaken in 2012/13.

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