

**Meeting:** Executive

Portfolio Area: Resources

**Date:** 18 July 2007

**TREASURY MANAGEMENT REVIEW 2006/07**

(Finance)

**NON-KEY DECISION**

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**1 PURPOSE**

To review the progress made towards achieving the objectives in the 2006/07 Treasury Management Strategy.

**2 RECOMMENDATIONS**

That Council be recommended to approve the 2006/07 Treasury Management Review.

**3 BACKGROUND**

- 3.1 It is a requirement of the Treasury Management Code of Practice that a report is presented to members of the Council to review the Treasury Management Strategy for the preceding financial year.
- 3.2 The Chartered Institute of Public Finance and Accountancy's Code of Practice on Treasury Management 2001 was adopted by the Council. The Council fully complies with the requirements of the Code.
- 3.3 The primary requirements of the Code are as follows:
- 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 Council of an annual strategy report for the year ahead (for 2006/07 this was reported to Council in February 2006) and an annual review report of the previous year (this report is intended to fulfil this requirement).

- 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.

## **4 REASONS FOR RECOMMENDED COURSE OF ACTION AND OTHER OPTIONS**

### **4.1 2006/07 Economic / Interest Rate Background**

4.1.1 The Base Rate started the 2006/07 financial year at 4.5%, having been unchanged at this level since August 2005. Monetary Policy Committee concerns that official data had been under recording the strength of economic growth were vindicated by retrospective adjustments (increases) to annual growth figures extending back as far as 2001 in the quarter 1 of 2006 Gross Domestic Product (GDP) figures. These revisions also increased the Q4 2005 and Q1 2006 GDP growth figures up from 0.6% to 0.7% quarter on quarter. This tipped previous expectations of an underperforming UK economy over into one that was running at or above its trend rate of growth. Previous expectations of cuts in Bank Rate in 2006 evaporated and were replaced by the reverse expectation i.e. at least one, if not two increases of 0.25% by the end of 2006. Bank Rate accordingly rose to 4.75% in August 2006 and then to 5.0% in November 2006.

4.1.2 This was followed by another rate increase in January 2007 to 5.25% which was a shock to both the financial markets and forecasters and immediately sparked inferences that the MPC had had access to adverse inflation news, which was not available to the markets at that time. This was subsequently confirmed by news that Consumer Price Inflation (CPI) had jumped to 3.0% in December. If this rate had risen above 3.0% the MPC would have had to write a letter of explanation to the Chancellor. The annual growth rate also hit 3.0%, the highest in two years, in Q4 of 2006, adding to confirmation that the increases in Bank Rate had done little to dampen the economy and stoking expectations that the Bank Rate would have to rise even further.

### **4.2 REVIEW OF 2006/07 STRATEGY**

4.2.1 When formulating the 2006/07 strategy, an interest return rate of 4.5% was estimated.

#### **4.2.2 External Fund Manager**

During 2006/07, the performance of the Fund Manager was kept under review due to its poor performance. The reviews were carried out by officers in conjunction with our Treasury Management advisors "Sector", who have access to performance benchmarking information for other fund managers active in the Local Authority market. Unfortunately, the performance of the External Fund did not recover as forecast. As a result, £12.5m was withdrawn from the External Fund to be managed Internally by the Council, where ongoing performance was generally more consistent. The £12.5m was brought back in-house during September and October, with the final tranche in December 2006. This timing was determined in order to allow certain External Fund investments to run to maturity rather than reduce the returns with premature repayment. At the end of the 2006/07 financial year the External Fund was managing £15.69m. The average return on the External Fund for 2006/07 was 4.14%. The External Fund Manager's performance has continued to be kept under review and a further £5m has been withdrawn to be managed in-house, during the early months of 2007/08.

#### 4.2.3 In-House Treasury Activity

At the end of the 2006/07 financial year, the Council's in-house treasury activity had £26.5m on deposit. Activity throughout the year, achieved an average return of 4.98%. These deposits are invested on the money markets in accordance with the Council's strict lending policies, which are formulate to ensure that, whilst the Council seeks to maximise its interest returns, the overriding importance is the security of the underlying investment. Hence the investment policy is very risk adverse. Determination of the Policy and day to day investment activities are supported with advice and market information provided by the Council's Treasury Management advisors "Sector".

#### 4.2.4 Funds Invested according to the Treasury Policy

All funds were invested according to the Treasury Management Policy. A list of the institutions used together with their credit ratings is attached (Appendix A). The overall return of the internal and external funds was 4.60% for the year.

#### 4.2.5 Treasury Management Prudential Indicators 2006/07

Prudential Indicators were introduced from 2004/05. These are defined by the CIPFA Prudential Code, under which the Council sets and monitors various Treasury Management limits for borrowing and lending activities. The original Indicators for 2006/07 were agreed by Council in February 2006. As a result of the funds being withdrawn from the External Fund and brought back in-house to manage, as referred to at paragraph 4.2.2 above, it was necessary to revise the 2006/07 Indicators and these updates were accordingly reported to Council in December 2006. It is the performance against the revised Indicators which is reported in the table below:

<b>Treasury Management Prudential Indicators</b>	<b>Approved Limits</b>	<b>Actual</b>
	£'000	£'000
<b>Sums invested at Variable Interest Rate</b>		
SBC	-10,000	-4,700
External Fund Manager	-29,000	-27,750
<b>Sums invested at Fixed Interest Rate</b>		
SBC	-40,000	-31,800
External Fund Manager	-31,000	-9,890
<b>Principal sums invested for over 364 days</b>		
SBC	20,000	3,200
External Fund Manager	31,000	9,890
<b>Borrowing Limits</b>		
Long term borrowing	15,000	0
Short term borrowing	15,000	0

## **5 IMPLICATIONS**

### **5.1 Financial Implications**

The report is of a financial nature and reviews the Treasury Management function for the 2006/07 financial year. Effective management of Treasury Activity, in accordance with the Treasury Management Policy, seeks to maximise the interest returns to the Council, whilst seeking to ensure the security of the Council's underlying investments.

### **5.2 Legal Implications**

None

### **5.3 Other Implications**

None

## **BACKGROUND DOCUMENTS**

- Treasury Management Reports
- Sector Reports
- Fund Manager Reports

## **APPENDICES**

- Appendix A - List of Institutions Used During the Year Ended 31<sup>st</sup> March 2007