

**REPORT TO:** Executive Board Sub-Committee

**DATE:** 9<sup>th</sup> September 2010

**REPORTING OFFICER:** Operational Director – Finance

**TITLE:** Treasury Management 2010/11  
1<sup>st</sup> Quarter: April – June

**WARDS:** Borough-wide

## **1.0 PURPOSE OF REPORT**

- 1.1 The purpose of this report is to update the Sub Committee about activities undertaken on the money market as required by the Treasury Management Policy.
- 1.2 CIPFA issued the revised Code of Practice for Treasury Management in November 2009. The revised code suggests members should be informed of Treasury Management activities at least twice a year, but preferably quarterly. This report therefore ensures Halton Borough Council is embracing Best Practice in accordance with CIPFA's revised Code.

## **2.0 RECOMMENDED: That the report be noted.**

## **3.0 SUPPORTING INFORMATION**

### **3.1 Economic Background**

The following has been provided by Sector, the Council's Treasury Management advisors:

The first quarter of 2010/11 saw:

- The new coalition government enacted a fiscal squeeze set to be the most severe since the end of the 1930's, through its Emergency Budget on the 22<sup>nd</sup> June 2010.
- Activity indicators suggested that the recovery picked up a little pace in the first quarter.
- High street spending recovered after a weak start to the year.
- The labour market showed some tentative signs of improvement.
- The UK's trade position deteriorated, despite the weak pound.
- Consumer Price Index (CPI) inflation remained above target; the measure of underlying inflation fell.
- The Monetary policy Committee (MPC) maintained Quantitative Easing and kept Bank Rate on hold at 0.5%.
- The recovery in the US remained fairly strong, but remained weak in the euro-zone.

The key development of the first quarter was the Emergency Budget delivered on 22<sup>nd</sup> June 2010 which unveiled plans to severely tighten fiscal policy – central government influencing the economy through spending and revenue collection mechanisms. The Office for Budget Responsibility forecast that cyclically adjusted net borrowing – the portion of borrowing that will not disappear with economic growth – will fall from 8.7% of GDP in the fiscal year just gone to 0.8% in 2014-15.

The Budget directed the bulk of the fiscal tightening at households and the public sector instead of private companies. Key measures within the Budget included a rise in the standard rate of VAT from 17.5% to 20%, to take effect in January 2011. Plans for social security payments were also scaled back. However, the burden on lower income households was partly offset by an increase in the income tax personal allowance by £1,000 to £7,475 from April 2011, from which high earners will not benefit.

Inflationary pressures have finally begun to ease. CPI inflation rose from 3.4% to a peak of 3.7% in April, before falling back down to 3.4% in May. Temporary factors such as the rise in the rate of VAT to 17.5% in January and the rise in oil prices last year, continued to support above-target inflation.

The MPC continued to keep Bank Rate on hold at 0.5% and to maintain its stock of asset purchases. The Bank of England's quarterly Inflation Report in May also projected inflation to be below the 2% target at the two year horizon, suggesting that rates will remain on hold for a considerable period. Some members of the MPC expressed concern that the recent bout of high inflation could lead to a permanent shift in inflation expectations if it persisted much longer.

### 3.2 Economic Forecast

The following forecast has been provided by Sector:

	NOW	Sep10	Dec10	Mar11	Jun11	Sep11	Dec11	Mar12	Jun12	Sep12	Dec12	Mar13
<b>Sectors Bank Rate View</b>	<b>0.50%</b>	0.50%	0.50%	0.75%	0.75%	1.00%	1.50%	2.00%	2.25%	2.75%	3.00%	3.50%
<b>5yr PWLB</b>	<b>2.29%</b>	2.50%	2.60%	2.80%	2.95%	3.20%	3.45%	3.80%	4.15%	4.40%	4.50%	4.65%
<b>10yr PWLB</b>	<b>3.58%</b>	3.80%	3.85%	4.00%	4.20%	4.40%	4.50%	4.70%	4.75%	4.90%	4.90%	5.05%
<b>25yr PWLB</b>	<b>4.31%</b>	4.45%	4.50%	4.55%	4.70%	4.80%	4.90%	5.05%	5.1%	5.20%	5.25%	5.25%
<b>50yr PWLB</b>	<b>4.29%</b>	4.45%	4.55%	4.60%	4.75%	4.85%	4.95%	5.05%	5.25%	5.25%	5.30%	5.30%

The forecast is based on moderate economic recovery and MPC inflation forecast being below target in two year's time.

The first Bank Rate increase is expected to be in 2011; and to reach 3.50% by March 2013.

There is considerable uncertainty in all forecasts due to the difficulties of forecasting the timing and amounts of QE reversal, the tough cuts outlined in the Emergency Budget and the speed of recovery of banks profitability and balance sheet position etc.

The balance of risks is weighted to the downside with the risk remaining of a double dip recession.

### 3.3 Short Term Rates

The bank base rate remained at 0.5% throughout the quarter.

	Start	April		May		June	
		Mid	End	Mid	End	Mid	End
	%	%	%	%	%	%	%
Call Money (Market)	0.50	0.54	0.55	0.55	0.55	0.55	0.55
1 Month (Market)	0.50	0.55	0.55	0.56	0.57	0.57	0.57
3 Month (Market)	0.60	0.65	0.68	0.70	0.71	0.73	0.73

### 3.4 Longer Term Rates

	Start	April		May		June	
		Mid	End	Mid	End	Mid	End
	%	%	%	%	%	%	%
1 Year (Market)	1.40	1.33	1.37	1.39	1.42	1.46	1.46
10 Year (PWLB)	4.26	4.31	4.20	4.02	3.83	3.80	3.64
25 Year (PWLB)	4.67	4.70	4.62	4.54	4.38	4.38	4.29

The PWLB rates are for new loans in the “lower quota” entitlements. Market rates are based on LIBOR rates published at the middle and end of each month.

### 3.5 Temporary Borrowing/Investments

Turnover during period

	No. Of Deals Struck	Turnover £m
Short Term Borrowing	3	10.70
Short Term Investments	23	50.03

Position at Month End

	April £m	May £m	June £m
Short Term Borrowing	0	0	0
Short Term Investments	18.35	26.60	27.78

During the period, short term investments have been used to meet expenditure in the early part of the year, rather than choosing to borrow at additional cost. Short term investments have increased during the

quarter with no short term borrowings outstanding at the end of the quarter.

#### Investment Income Forecast

The forecast income and outturn for the quarter is as follows:

	Cumulative Budget £'000	Cumulative Actual £'000	Cumulative Target Rate %	Cumulative Actual Rate %
Quarter 1	175	192	0.42	3.01
Quarter 2	251			
Quarter 3	273			
Quarter 4	275			

The Council's investment position has resulted from delays in the capital programme. As a result, investment income for the period is above budget profile.

The target rate is based on the 7-day LIBID rate. For comparison purposes the 1 month average rate was 0.44%, 3 month rate was 0.57% and the 6 month rate was 0.83%. The Actual rate exceeds the benchmark rate reflecting previous actions taken, to lock in a large proportion of the investment portfolio into longer dated fixed rate investments. When these investments unwind, the Council will not generate the same amount of income it has experienced in previous years.

### 3.6 Policy Guidelines

Interest Rate Exposure – complied with.

Approved Counterparty List – complied with.

Borrowing Instruments – complied with.

Prudential Indicators – complied with:

- Operational Boundary for external debt;
- Upper limit on interest rate exposure on fixed rate debt;
- Upper limit on interest rate exposure on variable rate debt;
- Maturity structure of borrowing as a percentage of fixed rate borrowing;
- Total principal sums invested for periods longer than 364 days;
- Maturity structure of new fixed rate borrowing

The Council continues to update its approved counterparty list to reflect the changes in credit worthiness of the organisations it lends to in line with its Treasury Management Practices.

#### **4.0 POLICY IMPLICATIONS**

4.1 None

#### **5.0 OTHER IMPLICATIONS**

5.1 None

#### **6.0 IMPLICATIONS FOR THE COUNCIL'S PRIORITIES**

##### **6.1 Children and Young People in Halton**

None

##### **6.2 Employment, Learning and Skills in Halton**

None

##### **6.3 A Healthy Halton**

None

##### **6.4 A Safer Halton**

None

##### **6.5 Halton's Urban Renewal**

None

#### **7.0 RISK ANALYSIS**

7.1 The main risks with Treasury Management are security of investment and volatility of return. To combat this, the Authority operates within a clearly defined Treasury Management Policy and annual borrowing and investment strategy, which sets out the control framework.

#### **8.0 EQUALITY AND DIVERSITY ISSUES**

8.1 There are no issues under this heading.

#### **9.0 LIST OF BACKGROUND PAPERS UNDER SECTION 100D OF THE LOCAL GOVERNMENT ACT 1972**

9.1 There are no background papers under the meaning of the Act.