Leicestershire County Council

CORPORATE GOVERNANCE COMMITTEE – 19TH FEBRUARY 2016

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

QUARTERLY TREASURY MANAGEMENT REPORT

Purpose of the Report

1. To update the Corporate Governance Committee about the actions taken in respect of treasury management in the quarter ended 31st December 2015.

Background

2. Treasury Management is defined as:-

   "The management of the organisation'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".

3. A quarterly report is produced for the Corporate Governance Committee to provide an update on any significant events in the area of treasury management.

Economic Background

4. The UK economy grew by a provisional estimate of 0.5% during the December quarter, which was slightly above the previous quarter's growth of 0.4%. Over the calendar year 2015 growth was an estimated 1.9%, which is a good result relative to most other areas of the world. There were increasing signs during the quarter, and since the quarter end, that the world economy is struggling and if this continues there will be an inevitable impact on UK growth.

5. UK inflation remained low, with Consumer Price Inflation – the Bank of England's target measure – standing at 0.2% in the year to December 2015. Although inflation is expected to tick up in the quarters ahead as some of last year's large decreases in fuel and energy costs drop out of the annual calculation, these increases are likely to be relatively modest. The Governor of the Bank of England has recently made it clear that he sees no prospects of increases to base rates for some time to come.

6. The biggest current concern to global growth is the significant slowdown that is occurring in China, as it adapts from an export-led economy to one based more on consumption. China is not the only emerging economy to be suffering a slowdown, so one of the potential engines of growth is definitely faltering. In December 2015 the US Federal Reserve raised interest rates for the first time since 2006, albeit by a small amount of 0.25%, in what was seen as a first move towards 'normalisation' of interest rates. It is possible that they will not raise rates any further for some time, given the lack of economic certainty elsewhere.

Action Taken during December Quarter

7. The balance of the investment portfolio decreased from £185.5m to £165.2m, although £7.5m of this decrease came as a result of an investment into a pooled property fund. After adjusting for this investment, the £12.8m reduction in the balance is normal and reflects the fact that fewer precepts and government grants were received in the third quarter of the financial year.

8. Activity during the quarter related mainly to the reinvestment of maturing loans with acceptable counterparties, and there was an attempt to lengthen the maturity profile as it appeared that the market was placing a higher-than-justified probability of a UK base rate rise in the middle of 2016. The £20m investment with Santander UK (in £15m and £5m tranches) was renewed with the same counterparty, but within a notice account rather than in money market loans. Using the 6 month notice account, and giving notice immediately, gave a substantial premium (1.15% vs. 0.75%) relative to a cash loan.

9. The impact of the action taking during the quarter was to increase the average rate of interest from 0.81% to 0.93%. Most of the increase came as a result of the new loans being at higher rates than the ones that matured although the reduction in the balance of cash held in Money Market Funds (from £20.5m to £10.2m) also had a meaningful impact, given that this cash earns a below-average rate within the portfolio of c.0.49%. How much money is held in Money Market Funds is a function of cash flows, availability of counterparties at attractive rates of interest and views on how future interest rates will change.

10. The loan portfolio at the end of December was invested with the counterparties shown in the list below.

	£m
Lloyds Banking Group/Bank of Scotland	45.0
Royal Bank of Scotland	50.0
Santander UK	20.0
Landesbank Baden-Wuerttemberg	10.0
Landesbank Hessen Thuringen	10.0
Close Brothers	10.0
Toronto Dominion Bank	10.0
Money Market Funds	10.2
	165.2

11. There are also five further loans with Lloyds Banking Group which are classified as ‘service investments’ for the Local Authority Mortgage Scheme (LAMS). These do not form part of the treasury management portfolio, but are listed below for completeness:
5 year loan for £2m, commenced 5th September 2012 at 2.72%
5 year loan for £1.4m, commenced 27th November 2012 at 2.19%
5 year loan for £2m, commenced 12th February 2013 at 2.24%
5 year loan for £2m, commenced 1st August 2013 at 2.31%
5 year loan for £1m, commenced 31st December 2013 at 3.08%

12. The Leicestershire Local Enterprise Fund has been making financing available to small and medium sized Leicestershire companies, via an association with Funding Circle, since December 2013. There are a number of hurdles that companies must clear before being able to access this funding, and any loans made will be classed as ‘service investments’. As such, these loans are not covered within the Treasury

Management Policy but at the end of December 2015 there had been 50 loans made totalling £492,400 and the average interest rate on these loans was 8.5%.

Resource Implications

13. The interest earned on revenue balances and the interest paid on external debt will impact directly onto the resources available to the Council.

Equality and Human Rights Implications

14. There are no discernible equality and human rights implications.

Recommendation

15. The Committee is asked to note this report.

Background Papers

None

Circulation under the Local Issues Alert Procedure

None

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