Agenda Item 11

Leicestershire County Council

CORPORATE GOVERNANCE COMMITTEE – 14 JUNE 2013

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 31 March 2013.

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 avoided a triple-dip recession as preliminary figures showed growth for the March quarter of 0.3%. However, economic output remains 2.6% below its peak of Q1 2008. Service industries were relatively strong and production was flat despite reductions in North Sea Oil output, but construction contracted.

5. Inflation remained stubbornly high, despite the weak economic environment. Despite the well-documented squeeze on disposable income, retail sales and consumer expenditure rose and the sometimes severe weather conditions did not appear to have a meaningful impact on spending.

6. Unemployment levels remained broadly static, but there was a slowdown in new jobs being created. The housing market appears to be resilient and the fall in mortgage rates, assisted by the Government's Funding for Lending Scheme (which provides cheap funding for financial institutions for on-lending), appears to be making the market more accessible for first-time buyers.

7. Three members of the Bank of England's Monetary Policy Committee voted in favour of further Quantitative Easing, clearly believing that the economy was in need of further assistance. The possibility of any increase in the Bank of England's base rate over the next 12 -18 months still appears to be remote.

8. The US economy continues to perform relatively well in an international context and the very clear intent of the new Japanese Government and the new Governor of the

Bank of Japan to stimulate demand and end the seemingly never-ending deflationary spiral there has been viewed universally as a positive move. Equity markets performed exceptionally well over the period, suggesting that investors were feeling more positive about the future, but history has shown that this sentiment can change very quickly and markets can erode months worth of gains within days if this happens.

Action Taken during March Quarter

9. During the March quarter three loans to the Bank of Scotland (part of the Lloyds Banking Group), totalling £25m and at rates between 2.5% and 3.1%, matured. Although our limits to Lloyds would have allowed us to renew the whole £25m, Lloyds limit the amount that they will borrow from any counterparty to £5m within any 'tranche' that they launch. As a result it was only possible to lend £20m of the maturing amount to Bank of Scotland and this was done by way of four different loans of £5m, all for one year and all at a rate of 1.1%. The remaining £5m of our limit to this counterparty was lent on 2nd April.

10. During the quarter, and after extensive talks with them, it was possible to set up an investment account with HSBC and to deposit £25m (our limit with them) into it. HSBC have been an acceptable counterparty throughout the financial crisis, but the rates that they were willing to pay for deposits meant that there were better opportunities for the money to be invested elsewhere. The new account will pay LIBOR (London Inter Bank Offer Rate) and we retain the ability to invest for 1 month or 3 months at the relevant LIBOR rate. The first investment, and the first renewal of investment at the end of March, were both placed for one month as there was no financial advantage to a three month deposit. The rates achieved have been broadly base rate (0.5%), but this is better than would be achieved if the money was left in the next best available option – Money Market Funds at about 0.35%.

11. The balance of the investment portfolio increased from £126.8m at the end of December 2012 to £141.4m at the end of March 2013. This volatility of balances is normal as many of our major cash flows are sizeable and the timing of them can impact noticeably onto balances. The average rate earned on the investments decreased substantially over the quarter from 1.48% to 1.02%. This reduction is a function of loans at attractive rates maturing and being reinvested at much lower rates – the downward trend in money market rates in recent months has been very substantial – and also the increase in the size of the portfolio, with the extra cash filtering naturally into Money Market Funds (because there are no other available counterparties) at rates that are well below the average for the portfolio. The rate is likely to reduce further over the quarters ahead, as existing loans mature and are replaced at a lower rate of interest.

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

	£m
Royal Bank of Scotland	20.0*
Barclays	5.0*
Lloyds Banking Group/Bank of Scotland	35.0
HSBC	25.0
Money Market Funds	56.4
	141.4

* Barclays and Royal Bank of Scotland are no longer acceptable counterparties and no further loans will be made to them following maturity.

13. The current list of acceptable counterparties is very short and comprises:

Lloyds Banking Group (£40m, for up to 1 year)
HSBC (£25m, for up to 2 years)
Local Authorities (£10m per Authority, for up to 1 year)
Money Market Funds (£25m limit per fund, maximum £125m in total)
UK Debt Management Office (unlimited, for up to 1 year)
UK Government Treasury Bills (unlimited, for up to 1 year)

14. There are also three further loans with Lloyds Banking Group which are classified as ‘service investments’ for the Local Authority Mortgage Scheme (LAMS), and one of these was placed during the quarter. These do not form part of the treasury management portfolio, but are listed below for completeness:

5 year loan for £2m, commenced 5 September 2012 at 2.72%
5 year loan for £1.4m, commenced 27 November 2012 at 2.19%
5 year loan for £2m, commenced 12 February 2013 at 2.24%

15. There were no changes to the external debt portfolio over the quarter.

Resource Implications

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

Equal Opportunities Implications

17. There are no discernable equal opportunity implications.

Recommendation

18. The Committee is asked to note this report.

Background Papers

None

<u>Circulation under the Local Issues Alert Procedure</u>

None

<u>Officers to Contact</u>

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