Leicestershire County Council

CORPORATE GOVERNANCE COMMITTEE – 2 SEPTEMBER 2013

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

QUARTERLY TREASURY MANAGEMENT REPORT

Purpose of Report

1. To update the Corporate Governance Committee about the actions taken in respect of treasury management in the quarter ended 30 June 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. During the quarter it became apparent, following the revision of previous figures, that the UK had never actually experienced a double-dip recession. This retrospective good news was bolstered with news that the UK economy had grown by 0.6% during the June quarter, which was a significant acceleration on previous growth.

5. Consumer spending, both on and off the High Street, grew at a pace that was encouraging and industrial production accelerated at its fastest pace since mid-2010. Whilst construction spending continued to fall, the pace of the fall was the lowest for almost 2 years and there are signs that the recovery is quite broad-based. Recent years have, however, seen growth in the first half of the year followed by a subdued second half to the year, so it is too early to be certain that the recovery is either meaningful or self-sustaining.

6. The Chairman of the Federal Reserve in the United States made comments during the quarter about the possibility of 'tapering' their asset purchase (i.e. quantitative easing) activities at an earlier point than had previously been anticipated, due to growth in the US showing signs of being sustainable. Despite the fact that he had already given assurances that the initiative would

remain in place until unemployment levels were reduced very substantially, markets took fright at this announcement and bond yields rose sharply and equity markets fell by 10%. Further comments gave markets some assurance that the reduction in activities was not imminent and equity markets recovered somewhat, but the sell-off gave an indication of how fragile confidence is in a sustainable recovery.

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. After the quarter end, the new Governor of the Bank of England, Mark Carney, stated that he intended to make the decision-making process of the Monetary Policy Committee (MPC) much more transparent and that there would be much clearer guidance given to markets about the likely future development of monetary policy. It appears clear that there is little prospect of an increase in the Bank base rate over the next 12 to 18 months, and that the stubbornly high inflation that is almost unique to the UK (other areas are battling the spectre of deflation) will not form any major part of the rate-setting process until there is sustained economic growth. Further it appears possible that factors other than inflation – currently the MPC's only target – will formally be adopted as part of the Bank of England's remit.

Action Taken during June Quarter

8. The balance of the investment portfolio increased from £141.4m at the end of March 2013 to £201.9m at the end of June 2013. Whilst it is normal for the balance to increase in the first quarter of the year, the extent of the increase was much larger than in previous years due to a change in the profile of the way in which certain grants are paid by Central Government. Balances are expected to fall gradually over the remainder of the year.

9. During the March quarter a two year loan of £5m with Bank of Scotland (part of the Lloyds Banking Group) that was paying 2.75% matured, as did a one year loan of £5m to Royal Bank of Scotland that was paying 2.25%. The only terms deposits placed were two separate one year loans of £5m to Bank of Scotland, both at a rate of 1.1%. All other activity related to movements within Money Market Funds and there were occasions in which loans had to be made to the Debt Management Office (at rates of 0.25%) because the limit of £125m with Money Market Funds was reached. Balances available for lending peaked at £247.1m on 28 May.

10. The average rate of interest earned on the investments decreased substantially over the quarter from 1.02% to 0.74%. This reduction is a function of loans at attractive rates maturing and being reinvested at much lower rates – there continues to be a downward trend in money market rates, but the extent of the falls is less than it has been over the last 6 to 9 months – 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 will reduce further over the quarters ahead, as existing loans mature and are replaced at a lower rate of interest.

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

	£m
Royal Bank of Scotland	15.0*
Barclays	5.0*
Lloyds Banking Group/Bank of Scotland	40.0
HSBC	25.0
Money Market Funds	116.9
	201.9

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

12. 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)

13. There are also three 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%

14. There were no changes to the external debt portfolio over the quarter, although a £12m loan (originally for four years at a rate of 2.80%) from the Public Works Loan Board matured on 1 July 2013. This maturity would have occurred on 30 June if it had not been a weekend, and the loan was not replaced.

Resource Implications

15. 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

16. There are no discernable equal opportunity implications.

Recommendation

17. The Committee is asked to note this report.

Background Papers

None

Circulation under the Local Issues Alert Procedure

None

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