

## **BRECKLAND COUNCIL**

### **Report of Lady K Fisher, Executive Member for Governance to the CABINET 09/09/2008**

#### **Treasury Management Performance and Prudential Indicators 2007/08**

##### **1. Purpose of Report**

- 1.1 The annual treasury report is a requirement of the Council's reporting procedures. It covers the treasury activity for 2007/08 and the actual Prudential Indicators for 2007/08.

##### **2. Recommendations**

- It is recommended that the Cabinet:
- 2.1 Approve the actual 2007/08 Prudential Indicators within the report  
2.2 Note the Treasury Management performance report for 2007/08  
2.3 Approve the MRP policy (3.2.3b)

**Note:** In preparing this report, due regard has been had to equality of opportunity, human rights, prevention of crime and disorder, environmental and risk management considerations as appropriate. Relevant officers have been consulted in relation to any legal, financial or human resources implications and comments received are reflected in the report.

##### **3. Information, Issues and Options**

###### **3.1 Background**

- 3.1.1 The annual treasury report is a requirement of the Council's reporting procedures. It covers the treasury activity for 2007/08 and the actual Prudential Indicators for 2007/08.
- 3.1.2 The report meets the requirements of both the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities. The Council is required to comply with both Codes through Regulations issued under the Local Government Act 2003.
- 3.1.3 This report summarises:
- The capital activity for the year
  - How this activity was financed
  - The impact on the Council's indebtedness for capital purposes
  - The Council's overall Treasury position
  - The reporting of the required prudential indicators
  - A summary of interest rate movements in the year
  - Debt and investment activity

###### **3.2 Issues**

- 3.2.1 During 2007/08 the Council complied with its legislative and regulatory requirements. The actual Prudential Indicators for the year, with comparators, are as follows:

<b>Actual Prudential Indicators</b>	<b>2006/07</b>	<b>2007/08</b>
Actual Capital Expenditure	£11.37m	£3.20m
Capital Financing Requirement	(£20.736)	(£19.039)
Financing Costs as a proportion of Net Revenue Stream	£0	£0

At 31 March 2008, the Council's external debt was £0 (£0 at 31 March 2007) and its investments totalled £40.3m (£36.8m at 31 March 2007).

### 3.2.2 The Council's Capital Expenditure and Financing 2007/08

3.2.2a The Council undertakes capital expenditure on long term assets. These activities may either be:

- Financed immediately through capital receipts, capital grants etc.; or
- If insufficient financing is available, or a decision is taken not to apply capital resources, the expenditure will give rise to a borrowing need.

3.2.2b The Council has previously fully financed its capital expenditure and does not therefore have a current borrowing need.

3.2.2c The wider treasury activities also include managing the Council's cash flows and the investment of surplus funds. These activities are structured to manage risk foremost, and then optimise performance. Wider information on the regulatory requirements is shown in Section 3.2.11.

3.2.2d The actual capital expenditure forms one of the required prudential indicators. The table below also shows how this was financed.

£m	2006/07 Actual	2007/08 Estimate	2007/08 Actual
Non-HRA capital expenditure	£11.37m	£12.98m	£3.20m
HRA capital expenditure	£0	£0	£0
<b>Total capital expenditure</b>			
Resourced by:			
Capital receipts	£0	£0	£0
Capital grants	£0.57m	£0.91m	£0.50m
Capital reserves	£10.80m	£12.07m	£2.70m
Revenue	£0	£0	£0
<b>Total Resources Applied</b>	<b>£11.37m</b>	<b>£12.98m</b>	<b>£3.20m</b>

### 3.2.3 The Council's Overall Borrowing Need

3.2.3a The Council's underlying need to borrow is called the Capital Financing Requirement (CFR). This figure is a gauge for the Council's debt position. This Council currently has a negative CFR, and so has no underlying need to borrow for a capital purpose.

3.2.3b With effect from 1 April 2008 the CLG introduced new Minimum Revenue provision (MRP) Guidance, which requires an MRP Policy to be approved by Members annually. The MRP is the mechanism for the reduction of the borrowing need by a revenue charge. The Council is not expected to have a borrowing need (a positive CFR) during 2008/09 and so an MRP policy is not currently required.

3.2.3c The Council's CFR for the year is shown below, and represents a key prudential indicator.

CFR (£m)	31 March 2007 Actual	31 March 2008 Actual
<b>Closing balance</b>	(£20.736)	(£19.039)

### 3.2.4 Treasury Position at 31 March 2008

3.2.4a It should be noted that the accounting practice required to be followed by the Council (the SoRP) changed in 2007/08 accounts and required financial instruments in the accounts (debt and investments etc) to be measured in a method compliant with national Financial Reporting Standards. The figures in this report are based on the amounts borrowed and invested and so may differ from those in the final accounts by items such as accrued interest.

3.2.4b During 2007/08 the Chief Accountant managed the debt position to £0 and the treasury position at 31 March 2008 compared with the previous year was:

Treasury position	31 March 2007		31 March 2008	
	Principal	Average Rate	Principal	Average Rate
<b>Total Debt</b>	<b>£0.00m</b>		<b>£0.00m</b>	
Fixed Interest Investments	£33.0m	4.96%	£29.0m	5.59%
Variable Interest Investments	£3.3m	4.75%	£11.325m	5.00%
<b>Total Investments</b>	<b>£36.3m</b>	<b>4.94%</b>	<b>£40.325m</b>	<b>5.42%</b>
<b>Net credit position</b>	<b>£36.3m</b>		<b>£40.325m</b>	

### 3.2.5 Prudential Indicators and Compliance Issues

3.2.5a Some of the prudential indicators provide either an overview or specific limits on treasury activity. These are shown below:

3.2.5b **Net Borrowing and the CFR** - In order to ensure that borrowing levels are prudent over the medium term the Council's external borrowing, net of investments, must only be for a capital purpose. Net borrowing should not therefore, except in the short term, have exceeded the CFR for 2007/08 plus the expected changes to the CFR over 2008/09 and 2009/10. Since the Council does not have a positive CFR, the Council's net investment position must be lower than the CFR. The Council has complied with this prudential indicator.

	31 March 2007 Actual	31 March 2008 Actual
<b>Net investment position</b>	<b>(£36.3m)</b>	<b>(£40.325m)</b>
<b>CFR</b>	<b>(£20.736m)</b>	<b>(£19.039m)</b>

3.2.5c **The Authorised Limit** - The Authorised Limit is the "Affordable Borrowing Limit" required by s3 of the Local Government Act 2003. The Council does not have the power to borrow above this level once set. The table below demonstrates that during 2007/08 the Council has maintained gross borrowing within its Authorised Limit.

3.2.5d **The Operational Boundary** - The Operational Boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the Boundary is acceptable subject to the Authorised Limit not being breached.

3.2.5e **Actual financing costs as a proportion of net revenue stream** - This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

	2007/08
<b>Original Indicator – Authorised Limit</b>	£1.0m
<b>Maximum gross borrowing position</b>	£0m
<b>Original Indicator – Operational Boundary</b>	£0m
<b>Average gross borrowing position</b>	£0m
<b>Financing costs as a proportion of net revenue stream</b>	0%

### 3.2.6 Economic Background for 2007/08

3.2.6a The rising trend in UK interest rates continued in the first half of the 2007/08 financial year. The domestic economic backdrop continued to present problems for the Monetary Policy Committee, notably in the early summer. CPI inflation breached the 3% upper limit of the Government's target range in April (reported in May), consumer spending growth remained buoyant and an expanding number of companies expressed intentions to raise prices.

3.2.6b Official Bank Rate was raised to 5.5% in May and 5.75% in July in response to the deteriorating inflation outlook. In addition, the Bank of England's May and August

Inflation Reports hinted that more hikes might be necessary.

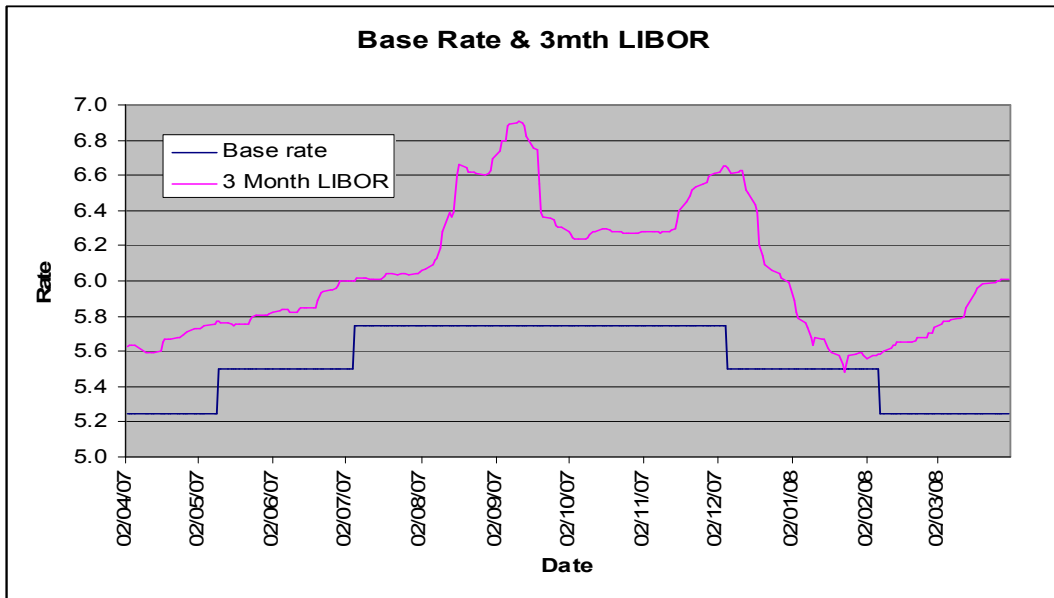
Interest Rates

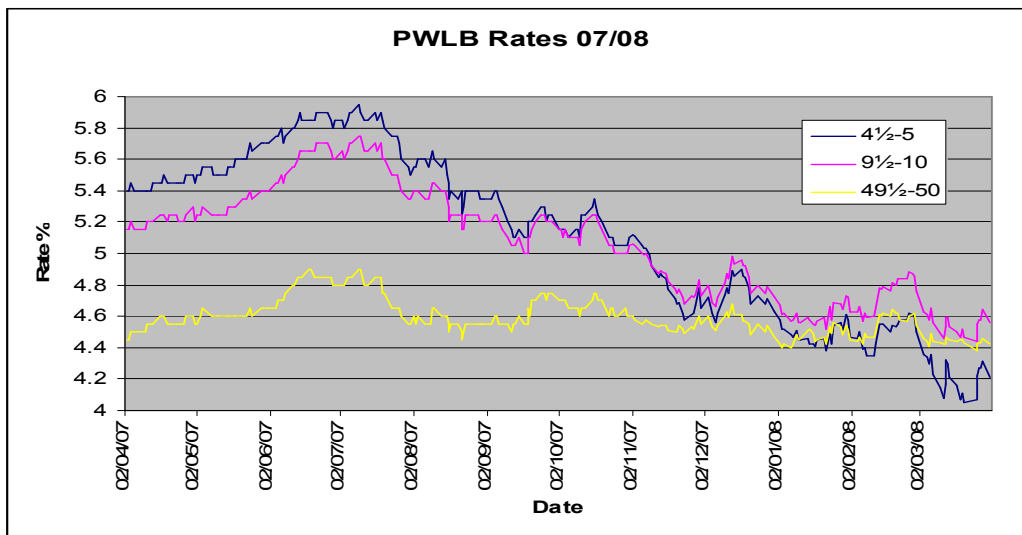
End Qtr	Bank Rate	LIBOR			PWLB Rates		
		3mth	6mth	1yr	5yr	20yr	50yr
2007 Mar	5.25	5.6	5.8	5.9	5.35	4.80	4.45
Jun	5.50	6.0	6.1	6.3	5.80	5.20	4.80
Sep	5.75	6.3	6.3	6.2	5.25	5.00	4.75
Dec	5.50	6.0	6.0	5.8	4.64	4.63	4.47
2008 Mar	5.25	6.0	6.0	5.8	4.14	4.70	4.43

3.2.6c The market was plunged into chaos in late August as the tightening of credit conditions, triggered initially by the failure of a selection of US mortgage lending institutions, undermined investor confidence. LIBOR rates rose to well over 6.5% as financial organisations' reluctance to lend money to counterparties sparked a severe shortage of funds in the market. In the UK, the crisis came to a head with the failure of the Northern Rock Bank (September) and while the danger of potential meltdown was defused by the Government's decision to guarantee all deposits with this institution, this failed to prevent a prolonged tightening of credit conditions.

3.2.6d Central banks strove to boost market liquidity via the injection of funds to the banking system and there were signs that this might be working in January. But a series of disappointing financial results and a persistent undercurrent of mistrust ensured a wide margin between official and market rates continued to year end.

3.2.6e The credit crisis provoked a significant change in the Bank of England's assessment of UK economic prospects over the medium term. It was clearly concerned that the tightening of liquidity and the consequent rise in borrowing rates across the entire economy could lead to a rapid slowdown in activity. This would help to contain inflation pressures. Bank Rate was cut by 0.25% on two occasions, December and February, to end the year at 5.25%.





### 3.2.7 The Strategy Agreed for 2007/08

3.2.7a The strategy provided for 2007/08 expected the treasury management operations would continue to be carried out within the framework of the medium term financial policy. It also highlighted an extraordinary treasury issue - acting as the accountable body for a number of grant funded projects. This required a rolling figure of £5m to accommodate partner cash flow requirements and Breckland's cash flow requirements.

### 3.2.8 Actual debt management activity during 2007/08

3.2.8a No borrowing was required during 2007/08.

### 3.2.9 Investment Position

3.2.9a **Investment Policy** – The Council's investment policy is governed by ODPM (now DCLG) Guidance, which has been implemented in the annual treasury management strategy approved by Council on 29 March 2007. The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

3.2.9b **Resources** – The Council's longer term cash balances comprise primarily revenue and capital resources, although these will be influenced by cash flow considerations. The Council's core cash resources comprised as follows, and meet the expectations of the budget:

Balance Sheet Resources (£m)	31 March 2007	31 March 2008
Balances	£12.457m	£12.830m
Earmarked reserves	£0m	£0m
Provisions	£0m	£0.04m
Usable capital receipts	£4.996m	£8.358m
Unapplied Grants and Contributions	£0.205m	£0.564m
<b>Total</b>	<b>£17.658m</b>	<b>£21.792m</b>

3.2.9c **Investments Held by Fund Managers** – The Council does not use Fund Managers currently to invest funds.

3.2.9d **Investments Held by The Council** - The Council does not have the expertise or resources to actively use a wide range of investment products and therefore performance tends to be more stable but lower over the longer term than for professionally managed funds (whose performance may fluctuate more). The Council maintained an average balance of £38m and received an average return of 5.42%. The comparable performance indicator is the average 7-day LIBID rate, which was 5.60%. This compares with a budget assumption of £28m investment balances at 5% interest rate.

### 3.2.10 **Performance Indicators set for 2007/08**

3.2.10a This service has set the following performance indicator:

- Investments – internal returns above the 7 day LIBID rate  
The actual performance for 2007/08 was 5.42% compared with a 7 day LIBID rate of 5.60% (see section 3.2.9d). The reasons behind this underperformance were:
- We have put security first, liquidity second and yield third when investing funds, this has been reflected in the rates achieved as higher rated counterparties tend to offer lower rates than the lower rated counterparties.
- We have kept some monies short term in order to fund our budgeted capital programme

### 3.2.11 **Regulatory Framework, Risk and Performance**

3.2.11a The Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
  - The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions were made in 2007/08);
  - Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act;
  - The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;
  - The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;
  - Under the Act the ODPM (now DCLG) has issued Investment Guidance to structure and regulate the Council's investment activities.
- Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices. Guidance on Minimum Revenue Provision was issued under this section on 8th November 2007.

3.2.11b The Council has complied with all of the above relevant statutory and regulatory requirements which limit the levels of risk associated with its treasury management activities. In particular its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach.

3.2.11c The Council is aware of the risks of passive management of the treasury portfolio and, with the support of Butlers, the Council's advisers, has proactively managed its treasury position.

## 3.3 Options

3.3.1 Approve the actual 2007/08 prudential indicators within the report and note the treasury management performance report for 2007/08.

3.3.2 Do not approve the actual 2007/08 prudential indicators within the report and note the treasury management performance report for 2007/08.

## 3.4 Reasons for Recommendation(s)

3.4.1 To comply with the Local Government Act 2003.

**4. Risk and Financial Implications**

4.1 Risk

4.1.1 [Insert statement as appropriate from Risk Questionnaire for Decision Makers – Author to draft but must clear report with risk manager]

4.2 Financial

4.2.1 None

**5. Legal Implications**

5.1 None

**6. Other Implications**

a) Equalities: None

b) Section 17, Crime & Disorder Act 1998: None

c) Section 40, Natural Environment & Rural Communities Act 2006: None

d) Human Resources: None

e) Human Rights: None

f) Other: None

**7. Alignment to Council Priorities**

7.1 This report is of a regulatory nature and therefore does not directly align with the Council's priorities.

**8. Ward/Community Affected**

8.1 N/a

**Background Papers**

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**Key Decision Status (Executive Decisions only):**

*This is not a key decision*

**Appendices attached to this report:**