APPENDIX

FALKIRK COUNCIL

Subject: **TREASURY MANAGEMENT ANNUAL REVIEW 2011/12**
Meeting: **POLICY & RESOURCES COMMITTEE**
Date: **4 September 2012**
Author: **CHIEF FINANCE OFFICER**

1. INTRODUCTION

1.1 Consistent with regulations issued under the Local Government in Scotland Act 2003 and the CIPFA Code of Practice on Treasury Management, an annual review of the Treasury Management Strategy must be prepared and submitted to the Policy and Resources Committee for scrutiny and thereafter considered and approved by full Council.

2. ECONOMIC AND INTEREST RATE REVIEW

2.1 The Treasury Management Strategy 2011/12, approved by Council in April 2011, noted that economic growth in the UK had faltered, with prospects for future growth remaining uncertain. The UK coalition Government has maintained a tight fiscal policy stance against a background of warnings from two credit rating agencies that the UK could lose its AAA credit rating. The USA and France lost their AAA credit ratings from one rating agency during the year.

2.2 The original expectation in 2011/12 was that the Bank Rate would start to rise to an average of 0.8% for the year. However, due to disappointing economic growth, including weak growth in our biggest export market – the EU, Bank Rate remained unchanged throughout the year. In addition, the Monetary Policy Committee increased quantitative easing by £75bn in October and another £50bn in February. At this time, Bank Rate is unlikely to rise until the second half of 2013 at the earliest.

2.3 In 2011/12 it was anticipated that medium and longer term rates would also start to rise and that short term rates would be the cheaper form of borrowing over the period. However, the movement in gilt yields meant that PWLB rates fell sharply during the year to historically very low levels. Rates for periods up to 5 years fell from 3.7% to 2.1% and for periods up to 25 years fell from 5.4% to 4.3%.

3. BORROWING STRATEGY 2011/12 – OUTCOME

3.1 The Council's longer term borrowing requirement for the year is set out below:

	2011/12 Original Estimate £m	2011/12 December Estimate £m	2011/12 Actual £m
Capital Programme (net of receipts)	26.7	26.4	24.1
Service Payments	(16.9)	(17.4)	(17.5)
Longer Term Loans maturing in year	0.5	0.5	0.5
Total Longer Term Borrowing Requirement	10.3	9.5	7.1

The reduction in the anticipated borrowing is due to the slippage in both the General and Housing Capital Programmes. The expenditure and related borrowing will now fall into the current financial year.

3.2 In the Strategy, it was noted that the Council's longer term borrowing requirement for the year was relatively low. As such, it was planned to take advantage of the significant rate differential in favour of funding linked to short term rates and/or longer term fixed rate periods of up to 5 years. The report also highlighted the potential for four Market Loans, up to a value of £26m, to be repaid during the year should any of the lenders invoke a rate change clause as per their contracts. Finally, it was recognised that significant cash outflows of £24m were required in respect of the Council's NPDO projects to provide four new high schools. These payments were funded from a mix of short term maturities and internal balances as detailed in the Treasury Management Annual Review 2010/11.

3.3 The interim report to Council on 23 January 2012 advised that the Council's estimated borrowing requirement remained outstanding. However, given the slippage in both the General and Housing Capital Programmes and the fact that we were able to utilise the Council's internal cash balances, this external borrowing did not take place.

The Market Loans referred to in para 3.2 remain on existing terms as lenders elected not to invoke contract break clauses.

3.4 There was no debt rescheduling activity during the year given the structure of long-term interest rates.

4. INVESTMENT STRATEGY

4.1 Members are reminded that the primary objectives of the Council's investment strategy remain first and foremost to ensure timeous and full repayment of principal and interest, then securing adequate liquidity of funds invested and finally optimising investment returns consistent with those counterparty risks.

4.2 Consistent with the requirement of the investment regulations and as part of its Strategy Report, Council approved a list of "Permitted Investments" setting out the types of investments to be used and monetary/time limits applied to each type of investment. It is confirmed that the Council did not breach any of the approved limits during the financial year.

4.3 There was no change to the counterparty selection criteria nor the list of eligible counterparties as advised in the Strategy Report to Council in April 2011.

4.4 The Council held £0.8m of investments, available on instant access in two UK Banks at 31 March 2012.

4.5 From 1 April 2011, new pensions legislation resulted in balances on behalf of the Pension Fund being held in a new Pension Fund bank account.

5. TREASURY MANAGEMENT PRUDENTIAL INDICATORS

5.1 Financing of the Capital Programme is a key driver of Treasury Management activities which in turn is managed by a series of treasury management prudential indictors. The purpose of the indicators is to contain the activity of the treasury function within specified limits, thereby managing risk and reducing the impact of an adverse movement in interest rates.

5.2 The three treasury indicators are set out at Appendix 1 and show comparison with the Council's actual exposure as at 31 March 2012. This confirms that the Council's treasury operations were operating well within the set parameters during financial year 2011/12.

6. MEMBER TRAINING

6.1 The Investment Regulations provide for increased scrutiny by Members of treasury management issues. To this end, a training session took place in June to which all Members were invited. This training session was tailored towards the needs and responsibilities of Members.

7. CONCLUSION

7.1 Treasury objectives consistent with the Strategy have been met in terms of both borrowing and investment. The legacy of the financial crisis means that market conditions remain challenging.

8. RECOMMENDATIONS

8.1 Committee notes the contents of the Annual Review 2011/12.
8.2 Refers the report to Council for consideration, consistent with regulations.

Chief Finance Officer

Date: 17 August 2012

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<u>LIST OF BACKGROUND PAPERS</u>

NIL

APPENDIX 1

TREASURY MANAGEMENT PRUDENTIAL INDICATORS

1. INTEREST RATE EXPOSURE

These limits set the maximum for fixed and variable interest rates based on the debt position net of investments and seeks to control the level of debt exposed to short term movements in interest rates.

	2011/12	
	UPPER LIMIT	**POSITION (31/03/12)**
Fixed Interest Rates	100%	93%
Variable Interest Rates	40%	7%

2. MATURITY STRUCTURE ON FIXED INTERST RATE BORROWING 2011/12

These gross limits are set to control the Council's level of exposure to loans expiring in any one period.

	Lower %	**Upper** %	**Position (31/03/12)** %
Under 12 months	0	25	14
12 months – 2 years	0	25	7
2 years – 5 years	0	50	0
5 years – 10 years	0	75	6
10 years – 20 years	0	75	11
20 years – 30 years	0	75	12
30 years – 40 years	0	75	24
40 years – 50 years	0	75	26

3. PRINCPAL SUM INVESTED > 364 DAYS

The Council does not place investments for periods longer than 364 days.