

**NORTH LANARKSHIRE COUNCIL**  
**AGENDA ITEM No. ....6.....REPORT**

To: POLICY & RESOURCES (FINANCE & CUSTOMER SERVICES) SUB-COMMITTEE		Subject: TREASURY MANAGEMENT MONITORING REPORT PERIOD 1 JANUARY TO 31 MARCH 2009
From: HEAD OF FINANCIAL SERVICES		
Date: 1 May 2009	Ref: PH/JQ/Q4	

### 1.0 Introduction

- 1.1 The purpose of this report is to inform on the quarterly activity (1 January 2009 to 31 March 2009) of the Council's loans and investment portfolios.

### 2.0 Background

- 2.1 The Council continues to manage its treasury activities in line with the CIPFA Code 'Treasury Management in the Public Services'. The Code requires the Council to produce reports on its Treasury Management policies, practices and activities on a regular and on-going basis. The Council fulfils these obligations in part by the preparation of a Treasury Management Monitoring report produced on a quarterly basis contained herein.
- 2.2 The Treasury activity undertaken in the final quarter of 2008/2009 reflects the key requirements of the Council's 2008/2009 Treasury Management Strategy, with the Public Works Loan Board and Long-term Money Market being the prime source of long-term funds. In addition, long term variable rate loans or temporary loans have not exceeded 25% of total borrowing. In terms of investment activity, all temporary lending is conducted with approved financial institutions.

### 3.0 Quarterly Activity

#### 3.1 Summary Position

- 3.1.1 The net overall borrowing position to 31 March 2009 is shown in Appendix 1. The balance of £399.2m represents an increase of £28.5m from the position at 1 January 2009 and was anticipated from the final quarter upsurge in the capital programme. In overall terms, this is a combination of several factors.
- 3.1.2 The primary reason is a planned reduction of £42.9m in the level of investment balances held at the end of the quarter, which is offset against the total loans outstanding. During the quarter under review, the Council, taking advantage of beneficial PWLB rates, used surplus cash balances to redeem £25.5m of PWLB debt early. The full extent of this debt rescheduling exercise is described later within the report. In addition, cash balances were used to meet daily revenue account requirements and to meet the capital financing requirement instead of borrowing for capital purposes.
- 3.1.3 The debt rescheduling exercise meant that there was a net reduction in the total loans outstanding of £14.4m, the £25.5m early debt redemption and £1.3m of principal on long-term loans repaid being partly offset by an increase of £8.9m in the bank overdraft falling due. The bank overdraft represents the level of BACS payments outstanding and cheques unrepresented as at 31 March 2009. There was also an increase of £3.5m in North Lanarkshire Municipal Bank deposits utilised by the Council.

## **3.2 Debt Restructuring**

- 3.2.1 As mentioned in 3.1.2 above, on-going monitoring of the economic climate and interest rate movements identified beneficial debt restructuring / rescheduling exercises, which were undertaken during the final quarter of 2008/2009.
- 3.2.2 In mid January 2009, £25.5m of PWLB loans were redeemed early using cash balances, with no replacement borrowing. These loans had interest rates ranging between 4.30% and 4.35% and they were due to mature during 2032/33 and 2053/55. The timing of the restructuring enabled the Council to redeem the loans without incurring a premium on early redemption. Indeed, the timing of the restructuring generated a one-off discount on early repayment of approximately £250k. With the discount being spread over 5 years, this will generate an annual saving of approximately £50k from 2009/2010 to 2013/2014. The net interest saved on these loans equates to £657k per year.
- 3.2.3 In March 2009, beneficial movements in PWLB interest rates provided the Council with the opportunity to redeem two PWLB loans early at par (no discount or premium due) and financed by a new 1 year loan at 0.78%. These loans totaled £5m with interest payable at 4.35% and were due to mature between 2032/2033 and 2033/2034. This will generate a one off saving of approximately £180k in annual interest payments, mainly in 2009/2010 and will reduce the average loans fund interest rate in 2009/2010.
- 3.2.4 The above restructuring exercises have resulted in financial savings. Equally important, they have also helped the Council to manage its Treasury risk in the current economic climate.
- 3.2.5 In the last six months, the global financial crisis has resulted in the credit rating of many financial institutions being downgraded. This has meant that the counterparty list of institutions that the Council can lend to has been reduced considerably as many no longer met our strict rating criteria. As previously advised to Committee, it was decided to reduce the Council's risk exposure by lowering the level of our investment balances to ensure a continued spread of investments across different counterparties and maturity periods.
- 3.2.6 Efficient cashflow management ensures that the early redemption of these loans will have no significant impact on the Council's liquidity and its ability to meet its service and business objectives on a daily basis.
- 3.2.7 Further reports regarding future activity will be presented to Committee as appropriate.

## **3.3. Borrowing**

- 3.3.1 During the quarter under review, as per 3.2.4 above, £5m of new long-term borrowing was undertaken.
- 3.3.2 As at 31 March 2009, short-term borrowing amounted to £29.9m, which represented an increase of almost £12.4m. This increase is accounted for by a rise of £8.9m in the bank overdraft and an increase of £3.5m in North Lanarkshire Municipal Bank deposits at the end of the quarter as described above.
- 3.3.3 During the normal course of business, day to day cash flow needs are examined and this resulted in cash movements both in terms of cash received and cash repaid. Short-term borrowing was used on only one occasion during the quarter with a total of £4.6m borrowed for three nights.

## **3.4 Short Term Investments**

- 3.4.1 In the fourth quarter of 2008/2009, positive cashflows enabled short-term investments of £162.4m to be undertaken. During the same period, approximately £205.3m of short-term investments carried forward from prior periods matured.
- 3.4.2 The net effect of these transactions was a decrease of £42.9m in investment balances as highlighted in paragraph 3.1.2.

### **3.5 Interest Rate Movements**

- 3.5.1 Following on from the previous quarter, from January to March 2009 there continued to be reductions in the Bank of England base rate, with the Monetary Policy Committee (MPC) taking the decision to reduce the base rate by 0.5% at each of its meetings over the three month period to the 31 March 2009. As a result, the base rate has fallen to 0.50% which is as low as the bank rate has been since the Bank of England was created in 1694.
- 3.5.2 The PWLB rates (25 year) have fluctuated considerably over the quarter rising as high as 4.86% in late January, before falling to a low of 3.99% in mid March, before settling at 4.28% at the end of the quarter. The short term (7 day) market rates which fell from 1.35% at the beginning of the quarter to 0.50% at the end of the quarter have been consistent with the official Bank of England base rate since the start of February.
- 3.5.3 Interest rates throughout the quarter over the medium to long term maturity spectrum, up to 50 years, have been fairly volatile due to the continuing fragility in the global financial markets amid uncertainty and a crisis of confidence.
- 3.5.4 The lower interest rate yields on investing, particularly in the short term, have had an impact upon the level of income earned from investing surplus cash balances. For example, yields available from investing surplus cash balances for 364 days have fallen from more than 6 % to 1.85%, with the 1 month fixed term deposit rate falling from 5.5% for the first quarter to 0.45% at the end of the fourth quarter.
- 3.5.5 Efficient cashflow management and prudent investment and borrowing activity ensured that the Council took advantage of the higher rates resulting in early year gains, the investment income levels remaining healthy in 2008/2009 when compared to budget. For 2009/2010, investment income budgets have been revised significantly downwards in line with current forecasts. This was incorporated within the Annual Treasury Strategy and Prudential Indicators for 2009/2010 and reported to Committee in March 2009.
- 3.5.6 The Treasury Management Section will continue to monitor financial and economic policy and their impact upon the Council's investment and borrowing activity.

### **4.0 The Prudential Code for Capital Finance in Local Authorities**

- 4.1 The Local Government in Scotland Act 2003 requires the Council to undertake its Treasury activities with regard to the Prudential Code for Capital Finance in Local Authorities.
- 4.2 Committee, at its meeting on 12 March 2008, approved a report titled, "Treasury Management Strategy 2008/2009 and Prudential Indicators 2008/2009 to 2010/2011". This report detailed a variety of mandatory and local indicators aimed at assisting members to determine that proposed capital investment levels and treasury management decisions satisfied the key requirements of affordability, prudence and sustainability. Performance against key prudential indicators for 2008/2009 is detailed within Appendix 2.
- 4.3 Committee will wish to note the following salient points:-
- (i) Indicator 1(a) illustrates that investment on capital expenditure was lower than expected due to slippage within the capital programme, which is monitored in detail as part of the Council's capital programme reporting mechanisms. This was matched by a reduction in the level of capital receipts generated, offset by additional cash grants and revenue contributions.
  - (ii) The Prudential Code requires the Council's capital investment to be affordable and prudent. To demonstrate this, a Prudential Margin (the need to borrow versus actual borrowing) is calculated. Indicator 1(b) demonstrates a healthy prudential margin as at the 31 March 2009. This is primarily due to early debt redemption of PWLB loan debt, reducing the net external debt (actual borrowing) with the surplus cashflow balances held financing these repayments.

- (iii) Indicator 2 illustrates that both the authorised and operational borrowing limit have not been exceeded, with the maximum borrowing undertaken within the period being well below the approved boundaries.
- (iv) Indicator 3(a) sets upper limits on the Council's exposure to the effects of interest rate changes by setting limits for each category of debt held (fixed or variable rate) which subsequently limits the Council's interest payable that is fixed or variable. At the end of the fourth quarter of 2008/2009, the actual levels remain below the limits for the fixed and variable interest rate exposure limits.
- (v) Indicator 3(b) highlights a reduction of £3.0m in net loan external interest payments compared to initial estimates for 2008/2009. External interest payments show a favourable variance of £1.5m, primarily due to lower borrowing costs as the Council, taking into account the current economic climate, sourced its capital financing requirement using cash balances held instead of seeking funds from the PWLB or the financial markets. The level of interest receivable on funds invested is expected to exceed budget by approximately £1.5m. This is due to an increase in the yields attained due to money market conditions in the early part of the year and also generally higher average surplus cashflows being available for investment in the first 6 months of the financial year. It should be noted, however, that interest rate yields have fallen by more than 75% in the last quarter in line with the significant cuts in the Bank of England base rate mentioned earlier. It should be noted that the table only includes external payments due and income receivable. Internal interest payable on revenue balances chargeable to the loans fund is expected to exceed budget by approximately £0.5m which, although a charge to the loans fund, will be matched by a corresponding credit to the General Fund and HRA.
- (vi) Indicator 3(c) relates to the level of fixed debt due to mature within time periods. The level of debt maturing remains within the upper limits set for each category at the beginning of the financial year.

4.4 The prudential indicators have remained in accordance with those approved by Committee on 12 March 2008. The projected final outturn illustrates a healthy prudential margin and borrowing levels that are below sustainable limits, ensuring that the projected capital investment levels remain affordable and sustainable.

4.5 As the year final accounting processes are completed, the net overall borrowing position and the prudential indicators reported above may be subject to minor change. Any subsequent amendments will be incorporated within the Annual Treasury Management Activity Report for 2008/2009 submitted to Committee later in the year.

## 5.0 Recommendation

5.1 It is recommended that Committee notes:

- (a) the treasury management activity for the quarter ended 31 March 2009 and the positive performance against key prudential indicators
- (b) the significant financial savings generated during 2008/09 and ongoing savings of £230,000 in 2009/10.



**Head of Financial Services**

*For further information please contact Joseph Quinn, Treasury Manager on tel ext 2061.*

**LOANS & INVESTMENTS AS AT 31 MARCH, 2009**

APPENDIX 1

	BALANCE 01-Jan-09	DEBT RESTRUCTURING		NEW BORROWING	PRINCIPAL REPAYMENTS	NET CASH MOVEMENTS	BALANCE 31-Mar-09
		EARLY REDEMPTION	REFINANCING				
<b><u>LONG-TERM LOANS</u></b>							
PWLB	321,943,500	(30,519,000)	5,000,000	0	(317,691)	0	296,106,810
MONEY MARKET LOANS	94,000,000		0	0	0	0	94,000,000
MUNICIPAL BANK	10,000,000		0	0	0	0	10,000,000
COVENANTS	1,917,590		0	0	(975,000)	0	942,590
OTHER LOCAL AUTHORITIES	68,500		0	0	0	0	68,500
	427,929,610	(30,519,000)	5,000,000	0	(1,292,691)	0	401,117,920
<b><u>SHORT-TERM LOANS</u></b>							
TEMPORARY	0		0	4,600,000	(4,600,000)	0	0
MUNICIPAL BANK	16,150,000		0	3,510,916	0	0	19,660,916
INTERNAL LOANS	6,280		0	0	0	0	6,280
BANK OVERDRAFT	1,243,750		0	8,948,559	0	0	10,192,309
	17,400,030		0	17,059,475	(4,600,000)	0	29,859,505
FINANCE LEASE OBLIGATIONS	165,000		0	0	(41,000)	0	124,000
<b><u>TOTAL LOANS OUTSTANDING</u></b>	<b>445,494,640</b>	<b>(30,519,000)</b>	<b>5,000,000</b>	<b>17,059,475</b>	<b>(5,892,691)</b>	<b>0</b>	<b>431,101,425</b>
<b><u>INVESTMENTS</u></b>							
CASH IN HAND	1,120,470		0	0	0	20,206	1,140,676
OUTSIDE AGENCIES INCL CALL & TRACKER A/CS	73,700,000		0	0	0	(42,900,000)	30,800,000
CLYDESDALE BANK - TELEBANK INVESTMENT A/C			0	0	0	0	0
<b><u>TOTAL INVESTMENTS O/STANDING</u></b>	<b>74,820,470</b>		<b>0</b>	<b>0</b>	<b>0</b>	<b>(42,879,794)</b>	<b>31,940,676</b>
<b><u>NET BORROWING</u></b>	<b>370,674,160</b>	<b>-30,519,000</b>	<b>5,000,000</b>	<b>17,059,475</b>	<b>(5,892,691)</b>	<b>42,879,794</b>	<b>399,160,740</b>

## Prudential Code for Capital Finance in Local Authorities

### 1. Capital Expenditure, Capital Financing Requirement and Prudential Margin

	<u>Initial Estimate</u> <u>2008/2009</u> <u>(£000s)</u>	<u>Projected Outturn</u> <u>2008/2009</u> <u>(£000s)</u>
(a) <b>Capital Expenditure</b>		
Total Spend	128,003	118,983
<b>Financed By:</b>		
Borrowing	57,333	57,137
Capital Receipts	50,287	21,052
Cash Grants	8,220	20,376
Capital from Current Revenue	12,163	20,418

	<u>Initial Estimate</u> <u>2008/2009</u> <u>(£000s)</u>	<u>Projected Outturn</u> <u>2008/2009</u> <u>(£000s)</u>
(b) <b>Prudential Margin Calculation</b>		
Capital Financing Requirement	484,508	471,764
Net Borrowing requirement	441,593	399,161
Prudential Margin	42,915	72,603

### 2. Authorised Limit and Operational Boundary

	<u>Authorised Limit</u> <u>2008/2009</u> <u>(£m)</u>	<u>Operational Boundary</u> <u>2008/2009</u> <u>(£m)</u>	<u>Maximum Borrowing Level Q4</u> <u>2008/2009</u> <u>(£m)</u>
Borrowing	514	499	444.40
Other Long-term Liabilities	1	1	0.20
Totals	515	500	444.60

### 3. Treasury Management Indicators

#### (a) Interest Rate Exposures

	<u>Upper Limits</u> <u>2008/2009</u> <u>(%)</u>	<u>Projected Maximum Exposure</u> <u>Limits held</u> <u>2008/2009</u> <u>(%)</u>
Fixed Interest Rates	105.00%	100.70%
Variable Interest Rates	25.00%	-0.70%

#### (b) Interest Payments and Income due on Loans Outstanding/Funds Invested

	<u>Initial Estimate</u> <u>2008/2009</u> <u>(£000s)</u>	<u>Projected Outturn</u> <u>2008/2009</u> <u>(£000s)</u>	<u>Variance</u> <u>(£000s)</u>	<u>%age</u>
Interest Payable on Fixed Rate Debt	23,902	22,586	-1,316	-5.51%
Interest Payable on Variable Rate Debt	4,502	4,344	-158	-3.51%
<b>Total External Interest Payments</b>	<b>28,404</b>	<b>26,930</b>	<b>-1,474</b>	<b>-5.19%</b>
External Interest Receivable	2,943	4,500	1,557	52.92%
<b>Net Loan External Interest Charges</b>	<b>25,461</b>	<b>22,430</b>	<b>-3,031</b>	<b>-11.91%</b>

#### (c) Maturity Structure of Borrowing

	<u>&lt;12months</u>	<u>12 months to 2 years</u>	<u>2 to 5 years</u>	<u>5 to 10 years</u>	<u>&gt;10 years</u>
Upper Limit maturing :Fixed Rate Debt	5.00%	5.00%	10.00%	25.00%	100.00%
Upper Limit maturing :Variable Rate Debt	0.00%	0.00%	0.00%	0.00%	25.00%
Maturity structure at the start of Q4	0.20%	0.46%	1.76%	17.54%	80.04%
Maturity structure at the end of Q4	1.80%	0.50%	2.56%	19.17%	75.97%