

COMMITTEE: Audit Committee	DATE: 30 March 2010	CLASSIFICATION: Unrestricted	REPORT NO.	AGENDA NO. 5.5
REPORT OF: Corporate Director of Resources ORIGINATING OFFICER(S): Oladapo Shonola, Chief Financial Strategy Officer		TITLE: Treasury Management Activity for Period Ending 28 February 2010 Ward(s) affected: N/A		

Lead Member	Cllr Ohid Ahmed – Resources and Performance
Community Plan Theme	All
Strategic Priority	One Tower Hamlets

1. SUMMARY

- 1.1 This report advises the Committee of treasury management activity for the year up to 28 February 2010 as required by the Local Government Act 2003.
- 1.2 The report details the current credit criteria adopted by the Corporate Director of Resources, the investment strategy for the current financial year and the projected investment returns.

2. DECISIONS REQUIRED

- 2.1 Members are recommended to note the contents of this report.

3 REASONS FOR DECISIONS

- 3.1 The Local Government Act 2003 and the Local Authorities (Capital Financing and Accounting) Regulations 2003 requires that regular reports be submitted to Council/Committee detailing the council's treasury management activities.
- 3.2 The regular reporting of treasury management activities should assist in ensuring that Members are able to scrutinise officer decisions and monitor progress on implementation of investment strategy as approved by Full Council.

4 ALTERNATIVE OPTIONS

- 4.1 The Council is bound by legislation to have regard to the Treasury Management (TM) Code. The Code requires that the Council or a sub-committee of the Council (Audit Committee) should receive regular monitoring reports on treasury management activities.
- 4.2 If the Council were to deviate from those requirements, there would need to be some good reason for doing so. It is not considered that there is any such reason, having regard to the need to ensure that Members are kept informed about treasury management activities and to ensure that these activities are in line with the investment strategy approved by the Council.

5 BACKGROUND

- 5.1 The Local Authorities (Capital Finance and Accounting) (England) Regulation 2003 requires local authorities to have regard to the Treasury Management (TM) Code. The TM code requires that the Council or a sub-committee of the Council (Audit Committee) should receive regular monitoring reports on treasury management activities and risks.
- 5.2 These reports are in addition to the mid-year and annual treasury management activity reports that should be presented to Council midway through the financial year and at year end respectively.
- 5.3 This report details the current credit criteria/risk level adopted by the Corporate Director of Resources, the investment strategy for the current financial year and the projected investment returns.

6. TREASURY ACTIVITY FOR PERIOD 1 April to 28 February 2010

- 6.1 This section of the report sets out:
- The current credit criteria being operated by the Council.
 - The treasury investment strategy for the current financial year and the progress in implementing this.
 - The transactions undertaken in the period and the investment portfolio outstanding as at 28 February 2010.

7 CREDIT CRITERIA

- 7.1 The following credit criteria for investment counterparties were established by the Council in February 2009 as part of the budget setting exercise. Explanation of credit ratings criteria is attached at Appendix I.

Table 1: Counterparty Credit Rating Criteria

	UK Institutions Up to £25M	UK Institutions Up to £10M	Overseas Institutions Up to £10M
Short Term	F1+	F1+	F1+
Long Term	AA-	AA-	AA-
Individual	B	BC	AB
Support	2	3	2

- 7.2 In response to the recent instability in capital markets and the banking sector the Corporate Director of Resources restricted the investment list to institutions which have guaranteed support from national governments who are assessed by the rating agencies as having the financial capacity to provide such support.

Table 2: Lending List

Institution	Country of Incorporation	Active in Market
Australia and New Zealand Banking Group Ltd	Australia	Y
Commonwealth Bank of Australia	Australia	Y
National Australia Bank Ltd	Australia	Y
Westpac Banking Corporation	Australia	Y
Dexia Bank Belgium	Belgium	Y
Overseas-Chinese Banking Corporation Ltd	China	Y
United Overseas Bank Ltd	China	Y
DBS Bank Ltd	Singapore	Y
Abbey National Plc (Santander Group)	UK	Y
Bank of Scotland Plc	UK	Y
Barclays Bank Plc	UK	Y
HSBC Bank Plc	UK	Y
Lloyds Banking Group Plc	UK	Y
National Westminster Bank	UK	N
Nationwide Building Society	UK	Y
Royal Bank of Scotland	UK	Y

8 INVESTMENT STRATEGY

- 8.1 Sector was appointed on a trial basis in February 2009 to provide a cash management service to the Council. The contract has now been awarded to Sector on a more permanent basis following a tendering exercise.
- 8.2 The service to be provided encompasses the development and implementation of an investment strategy with risk parameters specified by the Council and negotiating with counterparties the terms for term deposits of funds.
- 8.3 These functions were previously undertaken in-house but the Corporate Director of Resources considered it to be appropriate to move to external provision after the success of the trial.
- 8.4 The performance of the contractor will be closely monitored to ensure that the council's investment strategy is being followed and that returns are being maximised within the constraints of the strategy.
- 8.5 It should be emphasised that the Council retains control of the credit criteria and the investments. Sector's role is purely advisory.
- 8.6 Sector's interest rate projections are that base rate will remain static at 0.5% for the current financial year with no movement in rates until we are well into Q4 of 2010. Against this macro-economic perspective Sector has developed a strategy which delivers enhanced performance through maximising the investment term of the portfolio. This will enable the portfolio to obtain exposure to the higher rates associated with investment in the longer term.

- 8.7 Sector calculated that the Council will have an effective investment balance of £100million for 2009/10. This is an average and balances will vary through the year. The current balance of £79.8M reflects a reduction in balances due to significant capital expenditure and a lull in business rates collections in February and March 2010.
- 8.8 The current investment strategy within the constraints of the Councils credit criteria and liquidity requirement is as set out below.

Investment Strategy

Projection			Actual Deal			
Term	Amount £M	Rate %	Counterparty	Maturity	Amount £M	Rate
Overnight	15	0.75%	Abbey National plc	Call	10.000	0.80%
Overnight		0.75%	Clydesdale Bank plc	Call	12.400	0.75%
Overnight			Alliance & Leicester	Call		
Overnight		0.75%	Bank of Scotland plc	Call	12.400	0.75%
			SUB TOTAL		34.800	
1 Month	5	0.70%				
2 Months	10	1.00%				
3 Months	30	1.30%				
6 Months	5	1.60%	Nationwide	15 April 2010	5.000	0.80%
			Nationwide	15 July 2010	5.000	0.79%
9 Months	10	1.70%	Cater Allen (Santander)	01 March 2010	5.000	2.60%
			Nationwide	30 July 2010	5.000	0.99%
12 Months	25	2.00%	Cater Allen (Santander)	14 May 2010	5.000	3.00%
			Lloyds	12 August 2010	5.000	1.82%
			Cater Allen (Santander)	13 January 2011	5.000	2.20%
			Barclays Bank plc	27 April 2010	10.000	2.15%
			SUB TOTAL		45.000	
	£100		TOTAL		£79.800	

- 8.9 The council's bankers, the Co-operative Bank plc, are used as depositors of last resort for investment of additional funds received after the treasury transactions have been completed and the money markets have closed.

9 INVESTMENT RETURNS

- 9.1 As a result of investment decisions taken so far this year there has been a total return of £1.13M - a full year return of £1.237M is projected. This equates to 1.24% return on projected cash balances of £100M at the start of the year.
- 9.2 When compared against the following benchmarks: Bank of England base rate; 0.50%, 3 month LIBOR; 0.73%, 12 month deposit; 1.15%, the 1.24% return achieved compares favourably given that the strategy also relies on deposits to be placed in reserve accounts. Reserve accounts offer lower rates of return.

10. COMMENTS OF THE CHIEF FINANCIAL OFFICER

- 10.1. The comments of the Corporate Director Resources have been incorporated into the report.

11 CONCURRENT REPORT OF THE ASSISTANT CHIEF EXECUTIVE (LEGAL)

- 11.1 The Committee is asked to note the information in the report concerning the Council's treasury transactions undertaken by the Corporate Director of resources under delegated powers.

12. ONE TOWER HAMLETS CONSIDERATIONS

- 12.1 Interest on the Council's cash flow has historically contributed significantly towards the budget.

13. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

- 13.1 There are no Sustainable Actions for A Greener Environment implications.

14. RISK MANAGEMENT IMPLICATIONS

- 14.1 Any form of investment inevitably involves a degree of risk. To minimise risk the investment strategy has restricted exposure of council cash balances to UK backed banks or institutions with the highest short term rating or strong long term rating.

15 CRIME AND DISORDER REDUCTION IMPLICATIONS

- 15.1 There are no crime and disorder reduction implications arising from this report.

16 EFFICIENCY STATEMENT

- 16.1 Monitoring and reporting of treasury management activities ensures the Council optimises the use of its monetary resources within the constraints placed on the Council by statute, appropriate management of risk and operational requirements.

Appendix 1: Definition of Credit Ratings

Support Ratings

Rating	
1	A bank for which there is an extremely high probability of external support. The potential provider of support is very highly rated in its own right and has a very high propensity to support the bank in question. This probability of support indicates a minimum Long-term rating floor of 'A-'.
2	A bank for which there is a high probability of external support. The potential provider of support is highly rated in its own right and has a high propensity to provide support to the bank in question. This probability of support indicates a minimum Long-term rating floor of 'BBB-'.
3	A bank for which there is a moderate probability of support because of uncertainties about the ability or propensity of the potential provider of support to do so. This probability of support indicates a minimum Long-term rating floor of 'BB-'.
4	A bank for which there is a limited probability of support because of significant uncertainties about the ability or propensity of any possible provider of support to do so. This probability of support indicates a minimum Long-term rating floor of 'B'.
5	A bank for which external support, although possible, cannot be relied upon. This may be due to a lack of propensity to provide support or to very weak financial ability to do so. This probability of support indicates a Long-term rating floor no higher than 'B-' and in many cases no floor at all.

Short-term Ratings

Rating	
F1	Highest credit quality. Indicates the strongest capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.
F2	Good credit quality. A satisfactory capacity for timely payment of financial commitments, but the margin of safety is not as great as in the case of the higher ratings.
F3	Fair credit quality. The capacity for timely payment of financial commitments is adequate; however, near-term adverse changes could result in a reduction to non-investment grade.

Long-term Ratings

Rating	Current Definition (August 2003)
AAA	Highest credit quality. 'AAA' ratings denote the lowest expectation of credit risk. They are assigned only in case of exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.
AA	Very high credit quality. 'AA' ratings denote a very low expectation of credit risk. They indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A	High credit quality. 'A' ratings denote a low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher ratings.
BBB	Good credit quality. 'BBB' ratings indicate that there is currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity. This is the lowest investment-grade category

Individual Ratings

Rating	
A	A very strong bank. Characteristics may include outstanding profitability and balance sheet integrity, franchise, management, operating environment or prospects.
B	A strong bank. There are no major concerns regarding the bank. Characteristics may include strong profitability and balance sheet integrity, franchise, management, operating environment or prospects
C	An adequate bank, which, however, possesses one or more troublesome aspects. There may be some concerns regarding its profitability and balance sheet integrity, franchise, management, operating environment or prospects.
D	A bank, which has weaknesses of internal and/or external origin. There are concerns regarding its profitability, substance and resilience, balance sheet integrity, franchise, management, operating environment or prospects. Banks in emerging markets are necessarily faced with a greater number of potential deficiencies of external origin.
E	A bank with very serious problems, which either requires or is likely to require external support.