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Appendix 2 – The Council's Investment Position at 30th September 2011
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1 THE ISSUE

1.1 In February 2010 the Council adopted the 2009 edition of the CIPFA Treasury Management in the Public Services: Code of Practice, which requires the Council to approve a Treasury Management Strategy before the start of each financial year, review performance during the year, and approve an annual report after the end of each financial year.

1.2 This report gives details of performance against the Council's Treasury Management Strategy and Annual Investment Plan 2011/12 for the first six months of 2011/12.

2 RECOMMENDATION

The Cabinet agrees that:

2.1 the Treasury Management Report to 30th September 2011, prepared in accordance with the CIPFA Treasury Code of Practice, is noted

2.2 the Treasury Management Indicators to 30th September 2011 are noted.

2.3 this Treasury Management Report and attached appendices are reported to November Council.

3 FINANCIAL IMPLICATIONS

3.1 The financial implications are contained within the body of the report.

4 CORPORATE PRIORITIES

4.1 This report is for information only and therefore there are no proposals relating to the Council's Corporate Priorities.

5 THE REPORT

Summary

5.1 The average rate of investment return for the first six months of 2011/12 is 0.60% above the benchmark rate.

5.2 The Councils Prudential Indicators for 2011/12 were agreed by Council in February 2011 and performance against the key indicators is shown in **Appendix 1**. All indicators are within target levels.

5.3 The Council's Treasury Investments remain under constant review to ensure as a priority the protection of the capital sum invested, particularly in light of increasing concerns regarding Eurozone debt levels.

Summary of Returns

5.4 The Council's investment position as at 30th September 2011 is given in **Appendix 2**. The balance of deposits as at 30th September 2011 & 30th June 2011 is also set out in the pie charts in this appendix.

5.5 Gross interest earned on investments for the six months totalled £587k. Net interest, after deduction of amounts due to West of England Growth Points, PCT and schools, is £469k. **Appendix 3** details the investment performance, the average rate of interest earned over this period was 1.11%, which is 0.60% above the benchmark rate of average 7 day LIBID +0.05% (0.51%).

Summary of Borrowings

5.6 The Council undertook new borrowing totalling £30 million from the Public Works Loan Board during the quarter, taking total borrowing to £120 million. The decision was taken as borrowing rates moved below 5% due to concerns over the USA credit rating linked with delays in the Senate agreeing increases to the countries debt ceiling and continuing anxiety over Eurozone debt. The Council's Capital Financing Requirement (CFR) as at 31st March 2011 was £112.7 million with a projected total of £151 million by the end of 2011/12 based on the capital programme approved at February 2011 Council. The Capital Financing Requirement measures the Council's need to borrow to finance capital expenditure.

5.7 Following Local Government Reorganisation in 1996, Avon County Council's residual debt is administered by Bristol City Council. All successor Unitary Authorities make an annual contribution to principal and interest repayment, for which there is a provision in the Council's revenue budget. The amount of residual debt outstanding as at 31st March 2011 apportioned to Bath & North East Somerset Council is £16.43m. Since this borrowing is managed by Bristol City Council and treated in the Council's Statement of Accounts as a deferred liability, it is not included in the borrowing figures referred to in paragraph 5.5.

5.8 The current borrowing portfolio is shown in **Appendix 4**.

Strategic & Tactical Decisions

5.9 As shown in the charts in **Appendix 2**, the Council continued to tighten its risk appetite related to investments during the quarter due to increasing concerns about Eurozone debt and the impacts this could have on the banking sector. The approach included increasing the amounts invested with other Local Authorities, reducing exposure to foreign banks and suspending investments with lower rated UK Building Societies. The core strategy continued to be focussed on the higher rated UK banks & Building Societies that have either already or are likely to receive support from the UK Government should they experience financial difficulties. The amount invested with the Debt Management Office continues to remain between 0-10% of total investments. This approach will be kept under review going forward and investments with the debt Management Office could increase if risk levels increase.

5.10 Due to concerns related to the current Eurozone debt situation, the Council does not currently hold any investments with banks in countries within the Eurozone. The Council's investment counterparty list does not include any banks from the countries most affected by the debt situation in the Eurozone (Portugal, Ireland, Greece, Spain and Italy).

Future Strategic & Tactical Issues

5.11 Our treasury management advisors economic and market review for the first quarter 2011/12 is included in **Appendix 5**.

5.12 The Bank of England base rate has remained constant at 0.50% since March 2009.

Budget Implications

5.13 A breakdown of the revenue budget for interest and capital financing and the forecast year end position based on the period April to September is included in **Appendix 6**. This is currently forecast to be £250,000 favourable by the end of 2011/12.

6 RISK MANAGEMENT

6.1 The Council's lending & borrowing list is regularly reviewed during the financial year and credit ratings are monitored throughout the year. All lending/borrowing transactions are within approved limits and with approved institutions. Investment & Borrowing advice is provided by our Treasury Management consultants Sterling.

6.2 The 2009 edition of the CIPFA Treasury Management in the Public Services: Code of Practice requires the Council nominate a committee to be responsible for ensuring effective scrutiny of the Treasury Management Strategy and policies. In May 2010, the Council's treasury advisors provided training to the Corporate Audit Committee to carry out this scrutiny.

6.3 In addition, the Council maintain a risk register for Treasury Management activities, which is regularly reviewed and updated where applicable during the year.

7 EQUALITIES

7.1 This report provides information about the financial performance of the Council and therefore no specific equalities impact assessment has been carried out on the report.

8 RATIONALE

8.1 The Prudential Code and CIPFA's Code of Practice on Treasury Management requires regular monitoring and reporting of Treasury Management activities.

9 OTHER OPTIONS CONSIDERED

9.1 None.

10 CONSULTATION

10.1 Consultation has been carried out with the Deputy Leader of The Council & Cabinet Member for Resources, Section 151 Finance Officer, Chief Executive and Monitoring Officer.

10.2 Consultation was carried out via e-mail.

11 ISSUES TO CONSIDER IN REACHING THE DECISION

11.1 This report deals with issues of a corporate nature.

12 ADVICE SOUGHT

12.1 The Council's Monitoring Officer (Council Solicitor) and Section 151 Officer (Divisional Director - Finance) have had the opportunity to input to this report and have cleared it for publication.

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Sponsoring Cabinet Member	*Councillor David Bellotti*
Background papers	*2011/12 Treasury Management & Investment Strategy*
Please contact the report author if you need to access this report in an alternative format	

APPENDIX 1
Performance against Treasury Management Indicators agreed in Treasury Management Strategy Statement

1. Authorised limit for external debt
These limits include current commitments and proposals in the budget report for capital expenditure, plus additional headroom over & above the operational limit for unusual cash movements.

	2011/12 Prudential Indicator	2011/12 Actual as at 30th Sep. 2011
	£'000	£'000
Borrowing	201,000	120,000
Other long term liabilities	3,000	0
Cumulative Total	**204,000**	**120,000**

2. Operational limit for external debt
The operational boundary for external debt is based on the same estimates as the authorised limit but without the additional headroom for unusual cash movements.

	2011/12 Prudential Indicator	2011/12 Actual as at 30th Sep. 2011
	£'000	£'000
Borrowing	150,000	120,000
Other long term liabilities	2,000	0
Cumulative Total	**152,000**	**120,000**

3. Upper limit for fixed interest rate exposure
This is the maximum amount of total borrowing which can be at fixed interest rate, less any investments for a period greater than 12 months which has a fixed interest rate.

	2011/12 Prudential Indicator	2011/12 Actual as at 30th Sep. 2011
	£'000	£'000
Fixed interest rate exposure	**204,000**	**100,000***

* The £20m of LOBO's are quoted as variable rate in this analysis as the Lender has the option to change the rate at 6 monthly intervals (the Council has the option to repay the loan should the rate increase)

4. Upper limit for variable interest rate exposure
While fixed rate borrowing contributes significantly to reducing uncertainty surrounding interest rate changes, the pursuit of optimum performance levels may justify keeping flexibility through the use of variable interest rates. This is the maximum amount of total borrowing which can be at variable interest rates less any investments at variable interest rates (this includes any investments that have a fixed rate for less than 12 months).

	2011/12 Prudential Indicator	2011/12 Actual as at 30th Sep. 2011
	£'000	£'000
Variable interest rate exposure	**0**	**-75,400**

5. Upper limit for total principal sums invested for over 364 days
This is the maximum % of total investments which can be over 364 days.

	2011/12 Prudential Indicator	**2011/12 Actual as at 30th Sep. 2011**
	%	%
Investments over 364 days	**25**	**13**

6. Maturity Structure of new fixed rate borrowing during 2011/12

	Upper Limit	**Lower Limit**	**2011/12 Actual as at 30th Sep. 2011**
	%	%	%
Under 12 months	50	Nil	0
12 months and within 24 months	50	Nil	0
24 months and within 5 years	50	Nil	0
5 years and within 10 years	50	Nil	0
10 years and above	100	Nil	100

APPENDIX 2

The Council's Investment position at 30th September 2011

	Balance at 30th September 2011
	£'000's
Notice (instant access funds)	15,400
Up to 1 month	15,000
1 month to 3 months	10,000
Over 3 months	69,000
Total	**109,400**

The investment figure of £109.4 million is made up as follows :

	Balance at 30th September 2011
	£'000's
B&NES Council	93,673
West Of England Growth Points	4,848
Schools	10,879
Total	**109,400**

The Council had an average net positive balance of £105.0m (including Growth Points Funding) during the period April 2011 to September 2011.

Chart 1: Investments as at 30th September 2011 (£109.4m)

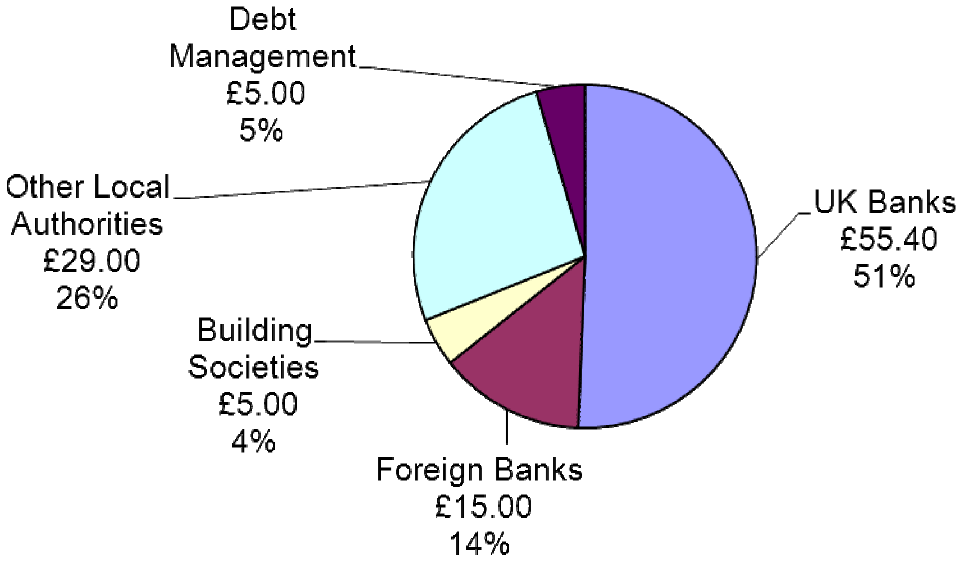


Chart 2: Investments as at 30th June 2011 (£90.8m)

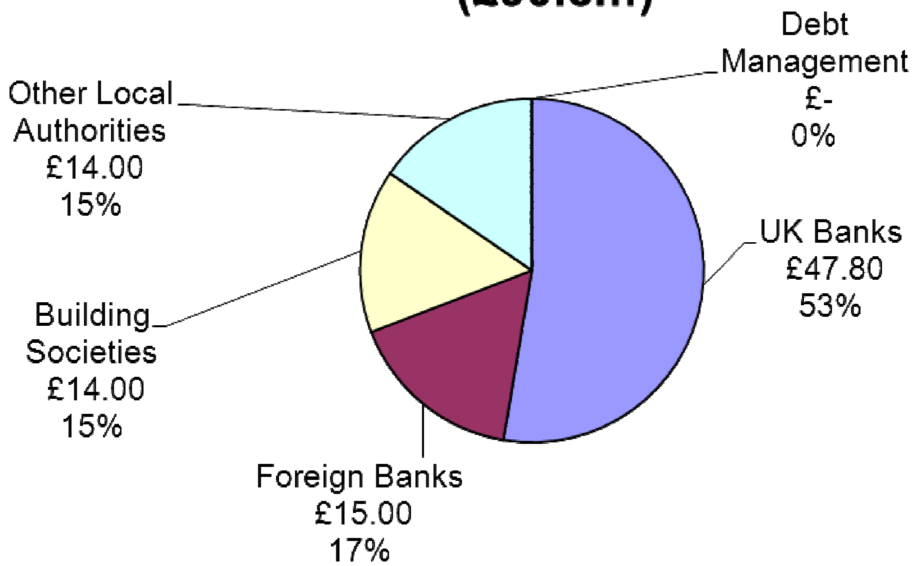


Chart 3: Investments per Lowest Equivalent Long-Term Credit Ratings (£109.4m) - 30th September 2011

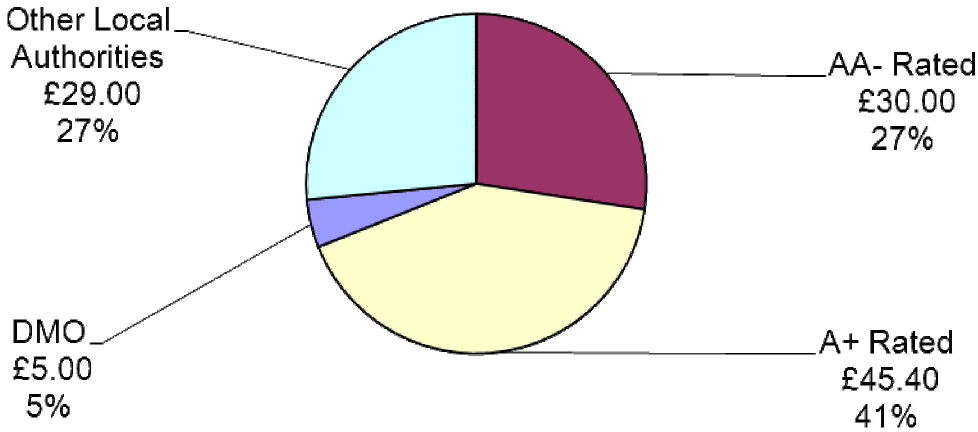
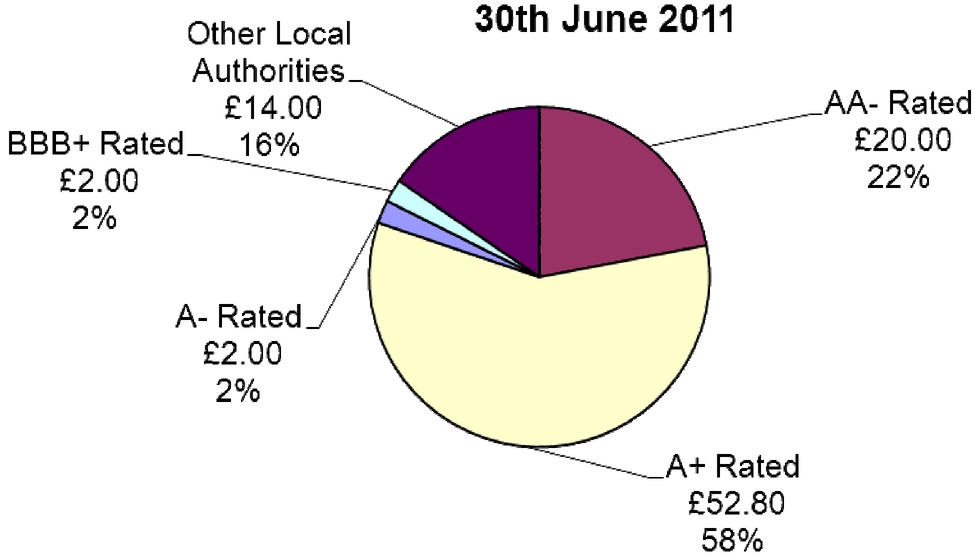


Chart 4: Investments per Lowest Equivalent Long-Term Credit Ratings (£90.8m) - 30th June 2011



APPENDIX 3

Average rate of return on investments for 2011/12

	April %	May %	June %	July %	August %	Sept. %	Average for Period
Average rate of interest earned	1.05%	1.13%	1.18%	1.10%	1.09%	1.14%	**1.11%**
Benchmark = Average 7 Day LIBID rate +0.05% **(source: Sterling)**	0.50%	0.50%	0.50%	0.52%	0.49%	0.54%	**0.51%**
Performance against Benchmark %	+0.55%	+0.63%	+0.68%	+0.58%	+0.60%	+0.60%	**+0.60%**

APPENDIX 4
Councils External Borrowing at 30th September 2011

LONG TERM	Amount	Fixed Term	Interest Rate	Variable Term	Interest Rate
PWLB	10,000,000	30 yrs	4.75%	n/a	n/a
PWLB	20,000,000	48 yrs	4.10%	n/a	n/a
PWLB	10,000,000	46 yrs	4.25%	n/a	n/a
PWLB	10,000,000	50 yrs	3.85%	n/a	n/a
PWLB	10,000,000	47 yrs	4.25%	n/a	n/a
PWLB	5,000,000	25 yrs	4.55%	n/a	n/a
PWLB	5,000,000	50 yrs	4.53%	n/a	n/a
PWLB	5,000,000	20 yrs	4.86%	n/a	n/a
PWLB	10,000,000	18 yrs	4.80%	n/a	n/a
PWLB	15,000,000	50 yrs	4.96%	n/a	n/a
KBC Bank N.V*	5,000,000	2 yrs	3.15%	48 yrs	4.50%
KBC Bank N.V*	5,000,000	3 yrs	3.72%	47 yrs	4.50%
Eurohypo Bank*	10,000,000	3 yrs	3.49%	47 yrs	4.50%
TOTAL	**120,000,000**				

*All LOBO's (Lender Option / Borrower Option) have reached the end of their fixed interest period and have reverted to the variable rate of 4.50%. The lender has the option to change the interest rate at 6 monthly intervals, however at this point the borrower also has the option to repay the loan without penalty.

APPENDIX 5
<u>Economic and market review for the six months to September 2011 (Sterling Consultancy Services)</u>

The first half of the financial year was characterised by deteriorating expectations for global economic growth and continued concern about sovereign creditworthiness, causing financial market volatility in August and September, as investors fled riskier assets for safe havens. Long-term gilt yields fell by a full percentage point to around 3.50% since their high in February.

Many Western developed nations, including the UK, implemented fiscal tightening policies to reduce public budget deficits, which unsurprisingly curbed domestic demand. At the same time, many economies were suffering from high inflation due to stubbornly high commodity prices; this prompted the European Central Bank (ECB) to raise interest rates in April and July.

The eurozone sovereign debt crisis proved the most significant influence on financial markets, with investors fearing the consequences of a sovereign default on the financial system. Despite the bailouts of Greece, Ireland and Portugal, the crisis rumbled on due to political differences that prevented concerted and conclusive action by the authorities. With a lack of firm policy direction from the centre, first Spain, then Italy faced difficulties, forcing the ECB to intervene and buy those countries' bonds in an effort to apply downward pressure on their funding costs. It also became apparent that Greece would require a second bailout if it was to avoid defaulting in 2013.

Meanwhile, concerns about the exposure of the interlinked European banking system to government debt caused funding conditions in interbank money markets to tighten. Sterling 3 month LIBOR rose to 0.95%, nearly double Bank Rate, in a situation reminiscent of the 2008 financial crisis. To avert another liquidity crisis, the world's major central banks offered unlimited loans to banks in September.

In the UK, the coalition government implemented its fiscal consolidation plan in the face of protests and public sector strikes, arguing that its decisive action has prevented a Greek-style crisis affecting the UK. Despite the resulting low confidence and subdued domestic spending, inflation remains high due to the rise in VAT and higher food and petrol prices. The Bank of England, however, was more concerned about the deteriorating economic outlook, and maintained Bank Rate at 0.5%, resisting pressure to increase rates to bring inflation back to target more quickly.

APPENDIX 6
Interest & Capital Financing Costs – Budget Monitoring 2011/12 (April to September)

April to September 2011	**YEAR END FORECAST** Budgeted Spend or (Income) £'000	Forecast Spend or (Income) £'000	Forecast over or (under) spend £'000	**ADV/FAV**
Interest & Capital Financing				
- Debt Costs	4,840	4,840		
- Internal Repayment of Loan Charges	(3,188)	(3,188)		
- Ex Avon Debt Costs	1,491	1,491		
- Minimum Revenue Provision (MRP)	3,380	3,380		
- Interest of Balances	(460)	(710)	(250)	FAV
Sub Total - Capital Financing	**6,063**	**5,813**	**(250)**	**FAV**