AUDIT COMMITTEE – 22 MARCH 2013

NEW FOREST DISTRICT COUNCIL

TREASURY MANAGEMENT PERFORMANCE REPORT – 1 APRIL 2012 TO 28 FEBRUARY 2013

1. INTRODUCTION

1.1 This is one of the regular reports on the Council's borrowing and investment activities that are submitted in accordance with the Treasury Management Code of Practice which the Council has adopted and applies its principles to all investment activity.

1.2 This report covers the period 1 April 2012 to 28 February 2013 for the Council's treasury management activities.

1.3 A glossary is attached as appendix 1.

2. STRATEGY FOR 2012/13

2.1 The Council approved the Treasury Management Strategy for 2012/13 in February 2012. This strategy is monitored by Council Staff on a daily basis.

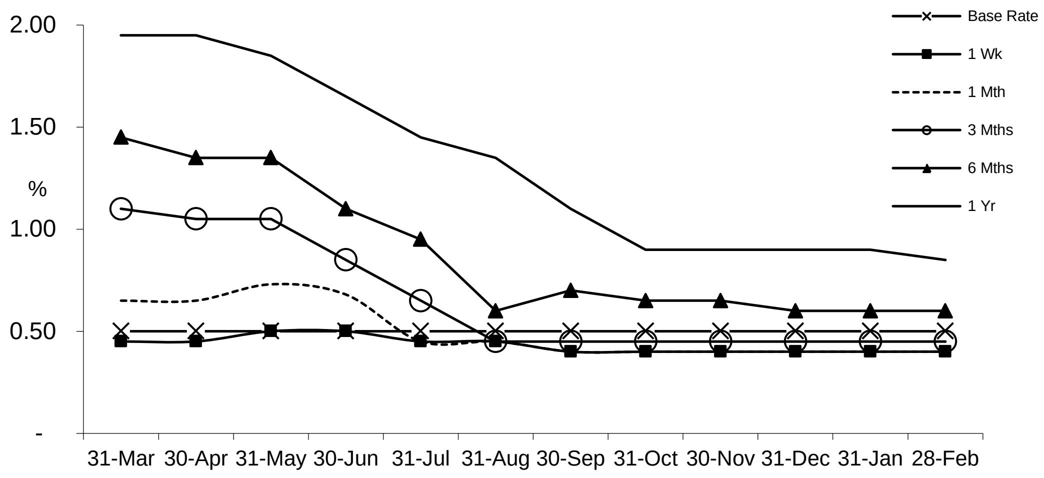
2.2 All financial advice provided by the Council's Treasury Consultants is given full consideration.

3. SUMMARY OF INTEREST RATES - to 28 February 2013

3.1 Investment Rates

3.1.1 Since April 2012, money market investment rates for one week to one year have varied between 0.40% and 1.95%.

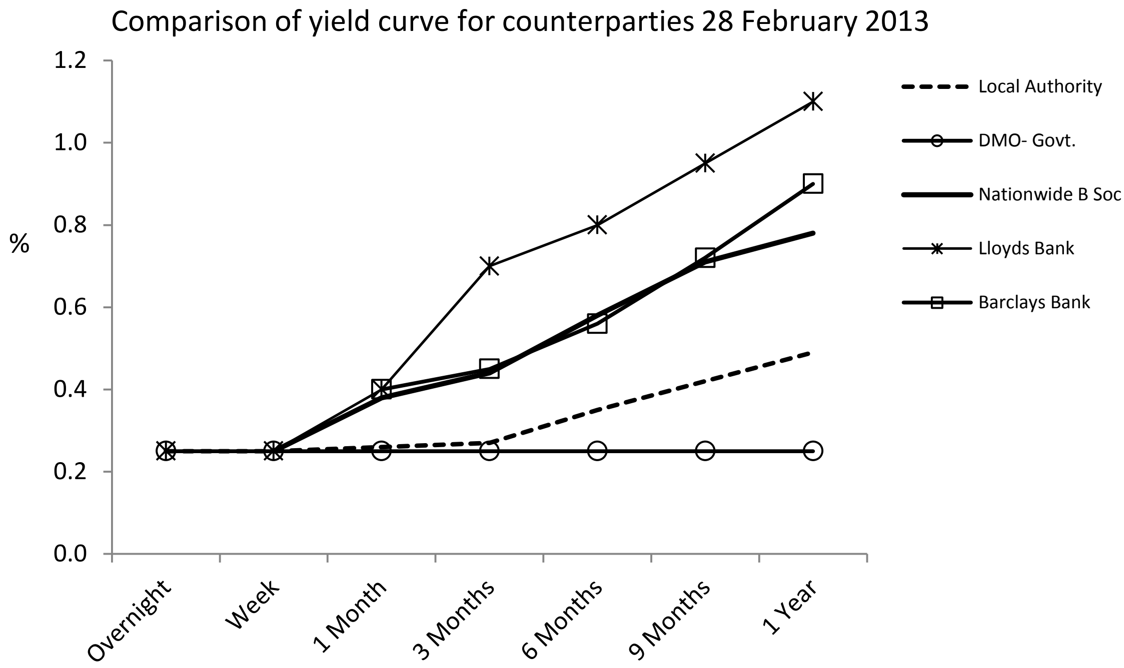
Money Market Interest Rates 1/4/12 to 28/02/13



3.1.2 The chart above reflects the average published money market rates that have been available over the period.

3.1.3 Money market investment rates have reduced over the year to date but have levelled out with no significant changes during the last five months.

3.1.4 Earlier in the year there was a large variation between one type of counterparty and another. However, these yields have now converged so that the difference has been greatly diminished. Examples of the current money market yield curves for different organisations are shown below.



3.1.5 There has been no change in the Bank of England base rate during the year to date:

Date	**Bank Base Rate**
At 1 April 2012	0.50%
28 February 2013	0.50%

4. ECONOMIC UPDATE

4.1 Global economy

Euro Zone

To date no country has availed itself of the ECB's support mechanism. Spain continues to hold out in the belief that their financial problems can be resolved without external aid. With recession, mass unemployment, and a huge public deficit the long term capability to avoid the need for help and accept the terms and conditions imposed, remains questionable.

Whilst Germany has avoided many of the problems of its partners the weight of the economic conditions within the EZ has affected its own economy.

There are also unresolved political problems in Italy. The Italian parliament convenes on 15th March when negotiations on the formation of a coalition government can begin.

The bloc is in recession and unemployment has reached a record high which will ensure that confidence in the region remains subdued. Domestic demand is weak and the strength of the Euro a potential threat to exports.

US

The year has started positively with politicians agreeing a deal on part of the "fiscal cliff" whilst deferring a decision on other parts of the problem until later in the year.

There are to be spending cuts in March but the ceiling has been extended until May when a strategy will need to be agreed. Two years ago delays caused the US to lose its AAA rating with S&P.

An estimate of a 0.1% contraction in Q4 GDP served as a stark reminder of the continued weakness of the US economy.

4.2 UK economy

Economic growth figures confirmed that Q4 GDP saw a contraction in growth. A decline of 0.3% was worse than expected. This increased the possibility that the UK economy could be heading toward a triple dip recession. Growth for 2013 looks set to be subdued at best.

The public finance figures strengthened the opinion that George Osborne may fall short of his deficit reduction target for the year. The UK has lost its AAA credit rating with Moody's

The labour market has proved resilient. Inflation held at 2.7% for a third month exceeding the MPC target level, but earnings growth has continued to fall below inflation leaving the prospect of weak consumer spending.

With the Euro Zone, the UK's largest trading partner, still in a debt crisis the prospects for significant improvement in exports look unlikely.

There has been some improvement in the UK housing market due mainly to the Funding for Lending scheme.

4.3 Outlook for the next six months of 2013

There remain uncertainties in economic forecasts due to the following difficulties:

- the continuing risk that the economy of the UK, US and EU will not grow substantially, or at all,

- the outcome of the US budget negotiations, and the threat of further spending cuts, is expected to impair investor and consumer confidence,

- volatility in Europe is likely to continue as many countries in the Eurozone are required to commit to long austerity measures to deal with their structural budget problems

- central UK government decisions are likely to continue to restrain funding and consumer growth.

The overall balance of risks is pessimistic:

- Low growth in the UK is expected to continue. The forecast increase in the bank base rate is not anticipated before 2015.

4.4 Interest rate forecast

The following table reflects the forecast of Sector Treasury Services who are the Council's treasury advisors.

Year	Base Rate	Money Market Rate		Borrowing Rate		
	%	3 Month %	1 Year %	10 year %	25-year %	50-year %
2013/14	0.50	0.5	1.0	2.9	4.1	4.2
2014/15	0.50	0.6	1.2	3.2	4.3	4.5
2015/16	1.25	1.4	2.3	3.8	4.8	4.9

5. LONG TERM BORROWING

5.1 The balance of long-term debt outstanding was £142.7m at 28 February 2013. None of this debt is scheduled to be repaid for the next 5 years.

5.2 The debt is running at an average annual percentage rate of 3.13%. A six monthly Interest payment of £2.2m is due on 28 March 2013.

6. TEMPORARY BORROWING AND INVESTMENT (SEE GLOSSARY)

6.1 Borrowing

6.1.1 Temporary borrowing is raised for cash flow purposes during the year.

6.1.2 However, no temporary borrowing has been raised during the year to date.

6.2 Temporary Investment

6.2.1 The revised budget for 2012/13 for interest receivable on temporary investments is £589,000 based on a revised average earnings estimate of 1.56% for the full financial year. The current forecast is £573,000 based on an estimate of £1.53%.

6.2.2 Funds of £17m which represent the Council's core funds, and is made up of reserves that are unlikely to be needed for expenditure during the rest of the year, have been invested in 12 month deposits. These earn a higher rate of interest than do deposits made for shorter periods.

6.2.3 Additional investments will be mainly for cash flow purposes and necessarily of shorter duration and hence will have lower rates of return.

6.2.4 A list of temporary investments at 28 February 2013 is shown at appendix 2.

7. INVESTMENT BENCHMARK

7.1 In order to measure the performance of the Council's investments the interest earnings are compared to a benchmark. The benchmark is established by taking a daily figure published by the money markets and averaging this over the year to establish an annual benchmark return.

7.2 The interest rate paid for those investments with durations of between 1 day and 3 months is compared to a benchmark that is compiled by averaging 7 day money at the London Interbank Bid (LIBID) rate over one year. The LIBID rate is the interest rate that major UK banks will pay for money deposits on the London Interbank market.

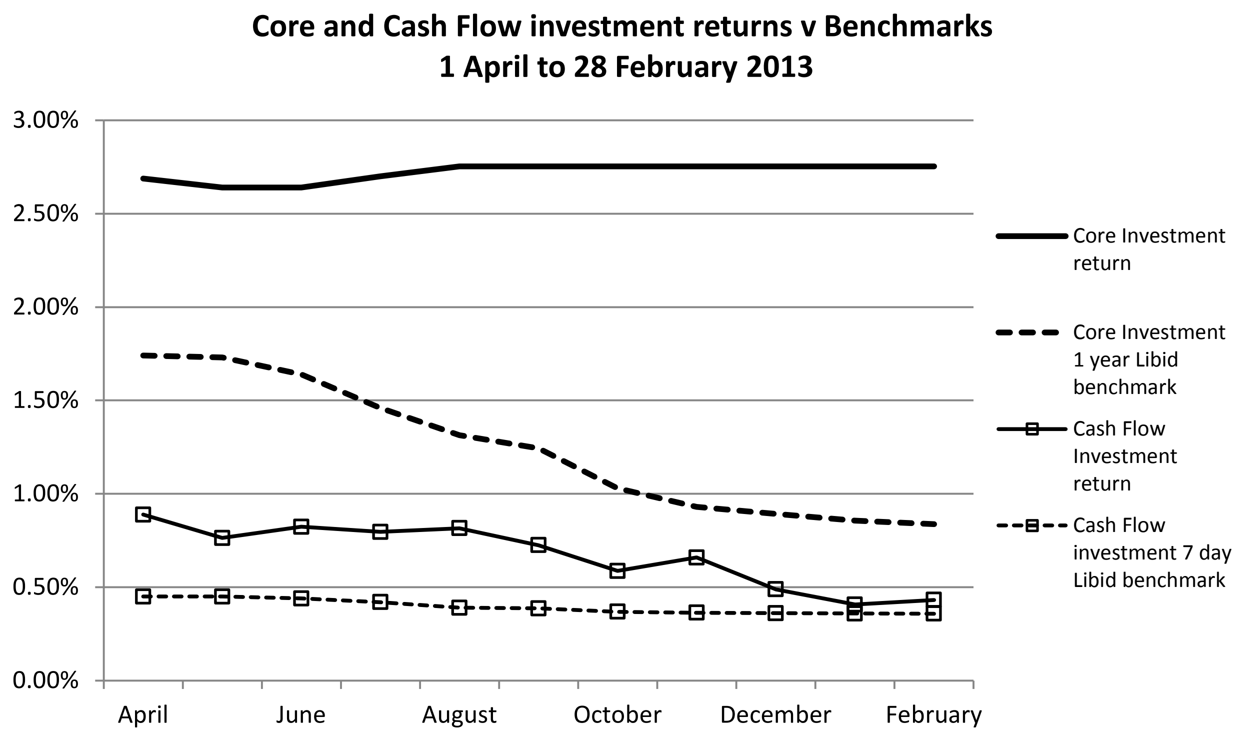
7.3 Because the Council invests over different periods the use of the 7 day benchmark, although widely used in comparisons, masks the performance of different ranges of investments. Therefore the Council also uses a benchmark of 1 year LIBID to compare the interest rate paid for those investments with duration of 1 year.

8. INVESTMENT CATEGORIES

8.1 In order to accurately appreciate the rate of return on investments it should be appreciated that there are two categories. One is for "cash flow" investments. These are the funds that are collected on behalf of the New Forest District Council, Hampshire County Council, Hampshire Police Authority and Hampshire Fire & Rescue. Some of these are paid out again in the form of a precept within a few weeks; some are used over a period of months. All will be used within the financial year and are not therefore available for strategic investment. Cash flow investments can be deposited in either short term deposits or instant access Money Market Funds and are compared to a 7 day LIBID benchmark.

8.2 The other category is for "core" investments. These are made from the Council's cash reserves which are unlikely to be used during the next 12 month period. These funds can be invested within the Treasury Strategy but with a mind to placing longer term deposits and therefore achieving a higher rate of interest. These are compared to a 1 year LIBID benchmark.

8.3 The following graph compares the different investment returns and their respective benchmarks:-



8.4 At the 28 February 2013 investments that were placed in instruments with a one year duration initially totalled £17m, and shorter term investment totalled £19m.

8.5 The details of these investments are shown at appendix 2.

9. INVESTMENT INSTRUMENTS

9.1 All investments have been made in Bank, Building Society or UK Government deposits or in Money Market Funds.

9.2 All deposits earn a yield that is made up entirely of interest earnings. There is no capital appreciation. No Gilts or Certificates of Deposits are traded.

10. INVESTMENT STRATEGY AMENDMENTS

10.1 There have been no amendments required to the overall investment strategy in 2012/13.

10.2 However, with the ongoing problems in the banking world the Council is currently operating a much more limited working investment strategy than the one approved in February 2012.

10.3 The current working practice is that investments are limited to the counterparties shown in the following table. Investments are restricted both in the sum invested in each institution and the term of the deposit. This list is regularly reviewed at monthly investment meetings.

Counter-party	Credit Rating	Element of UK Government Control	Maximum Investment	Maximum Term	Comments
Lloyds	A	Yes	£10m	1 year	
Barclays	A	No	£10m	3 Months	
HSBC	AA	No	£10m	3 Months	
RBS Group (NatWest/ RBS)	A	Yes	£10m	1 year	Group limited to £10m.
Nationwide	A+	No	£10m	3 Months	
DMO	AAA	Yes	£10m	1 year	UK Government
Other Local Authorities	AAA	Yes	£10m per Authority	1 year	Not rated but deemed AAA.
MMF	AAA	No	£10m per MMF	n/a	Instant Access

11. BORROWING STRATEGY AMENDMENTS

11.1 There have been no amendments required to the borrowing strategy.

12. COMPLIANCE WITH THE CIPFA CODE OF PRACTICE

12.1 All treasury functions and debt management procedures, which were undertaken during the period, complied with the existing CIPFA Code of Practice on Treasury Management, as set out in the Council's Treasury Policy Statement, and the Treasury Management Strategy for 2012/13.

13. ENVIRONMENTAL IMPLICATIONS

13.1 There are no environmental implications arising from this report.

14. CRIME AND DISORDER IMPLICATIONS

14.1 There are no crime and disorder implications arising from this report.

15. CONCLUSIONS

15.1 The current forecast for temporary interest earnings is £573,000, slightly less than the revised budget of £589,000.

15.2 The interest earnings have been in excess of the benchmarks for both the core and the temporary investments.

15.3 Interest rates for investments have stabilised over the last few months after reducing significantly in the first part of the year.

15.4 No long term borrowing has been undertaken during the period.

15.5 The current working investment practice is more limited than the approved Treasury Strategy for the year.

15.6 The current UK and global economic situations are unlikely to improve dramatically in the near future.

15. RECOMMENDATIONS

It is recommended that:-

15.1 Members note the performance of the treasury management function for the period from 1 April 2012 to 28 February 2013.

Further Information
Please contact Jan Hawker, Treasury Management Accountant Ext. 4444
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Background Papers
Published Papers

jsh/tmperfebruary2013

APPENDIX 1

GLOSSARY OF TERMS

BASE RATE

This is the minimum lending rate of a bank or financial institution in the UK. In this report the Base Rate refers to the Bank of England Base Rate.

BENCHMARK

A measure against which the investment policy or performance of a fund can be compared.

CERTIFICATES OF DEPOSIT

This is evidence of a deposit with a specified bank of building society that is repayable on a fixed date. They are negotiable instruments and have a secondary market; therefore the holder of a CD is able to sell it to a third party before its maturity.

COUNTERPARTY

The other party to an agreement or contract (e.g.: the lender or borrower).

DEBT MANAGEMENT OFFICE (DMO)

The DMO offers a Debt Management Account Deposit Facility which provides councils with a flexible and secure facility to supplement their existing range of investment options. The DMO is a Government Office and therefore has the highest possible credit rating. The DMO pay a very low rate of interest to councils depositing funds with this facility.

GILT

A Gilt is a registered British government security that gives the investor an absolute commitment from the government to honour the debt that those securities represent.

MONEY MARKET FUND (MMF)

A pool of cash which is managed by an independent fund management company. Frequently these are well known banks or investment houses. Investors purchase units of the fund which are held on their behalf in a custody account. These funds have the highest possible credit rating.

TEMPORARY BORROWING AND INVESTMENT

Loans which are capable of being repaid within one year. The term of the loans will be negotiated from overnight to 364 days.

TERM DEPOSIT

A deposit held in a financial institution for a fixed term at a fixed rate.

APPENDIX 2

TEMPORARY INVESTMENTS OUTSTANDING AT 28 FEBRUARY 2013

Institution	Amount of Investment £	Interest Rate %	Start Date	Maturity Date
Nationwide Building Society	2,000,000	0.44	03.12.12	04.03.13
Barclays Bank PLC	3,000,000	0.46	28.12.12	28.03.13
Barclays Bank PLC	1,000,000	0.46	28.12.12	28.03.13
National Westminster Bank PLC	2,000,000	2.25	05.04.12	04.04.13
Lloyds TSB Bank PLC	7,000,000	3.15	11.04.12	11.04.13
National Westminster Bank PLC	3,000,000	2.25	23.05.12	23.05.13
Lloyds TSB Bank PLC	3,000,000	3.00	23.07.12	04.07.13
National Westminster Bank PLC	2,000,000	2.25	17.08.12	16.08.13
IGNIS Money Market Fund	10,000,000	0.45	Instant	Access
Prime Rate Money Market Fund	2,600,000	0.40	Instant	Access
	35,600,000			