

Treasury Management Monitoring Report 2010/11

1. Summary

- 1.1. This report sets out the mid-year review of treasury management activities during 2010/11.

2. Contextual information

- 2.1. Hampshire Fire & Rescue Authority fully complies with the requirements of the revised CIPFA Code of Practice for Treasury Management in the Public Services (2009).

- 2.2. In the light of the Icelandic bank situation in 2008, CIPFA has amended the Treasury Management Code which introduces a new requirement for a mid-year review.

- 2.3. Treasury management in the context of this report is defined as:

“The management of the organisation’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.” (CIPFA Code of Practice).

3. Investments

- 3.1. During the first six months of 2010/11, cash flow requirements have meant that there is no scope for any direct long-term investment on the money markets. Therefore, the Authority has invested all its surplus funds with the County Council, earning interest based on the seven-day notice rate of 0.30%. When the position is overdrawn, the interest rate payable is similarly based on the seven-day notice rate.
- 3.2. At the Finance & General Purposes Committee meeting on 15 January 2009, it was agreed that the interest rate receivable on surplus cash balances would be based on the seven-day notice rate and that any capital losses on pooled cash balances would be shared on a pro rata basis.
- 3.3 The seven-day notice rate has historically been seen as a reasonable rate for short-term, low value cash surpluses and has broadly aligned to the Bank of England's base rate as can be seen as follows:

	Average base rate	Average seven-day notice rate
2006/07	4.8	4.9
2007/08	5.6	5.7
2008/09	3.5	3.7
2009/10	0.5	0.3
2010/11	0.5	0.3

- 3.4 However, the banking sector liquidity crisis since Autumn 2008 has meant that the seven-day notice rate is no longer a good measure of risk and reward. Going forward, changes to banking regulations will adversely impact this seven-day notice rate as short notice monies will not count towards banks' minimum required capital ratios. An alternative could be to move to the Bank of England's base rate. Therefore, the Authority might want to review the basis for calculating interest on its surplus or overdrawn cash position for future years
- 3.5 The Authority started the year in a cash deficit position of £3.2m and whilst fluctuating considerably throughout the period, a grant reimbursement relating to previous years' pensions expenditure received in July 2010 moved the cash balance into a surplus of £8.2m, although this has since declined to £6.4m as at 30 September 2010.
- 3.6 The extent of cash balances will continue to diminish between now and the end of the financial year, due to a combination of ongoing capital spending being funded from borrowing and the pensions grant being drawn down.
- 3.7 The annual strategy report presented to the Hampshire Fire & Rescue Authority on 10 February 2010 suggested that a weak economic recovery would limit the requirement for the base rate to increase from 0.5%, with market forecasts at the time indicating a base rate level of 1.0%, 2.0% and 3.0% by the ends of 2010, 2011 and 2012 respectively.
- 3.8 A slowing global economy and a weaker outlook for UK economic growth due to Government spending cuts and higher taxes means that despite inflation being above the Bank of England's 2.0% target (3.1% for the year ended August 2010) and forecasted to remain around 2.7% in 2011, the market forecasts have become rather more subdued indicating a base rate level of 0.5%, 1.5% and 2.5% by the ends of 2010, 2011 and 2012 respectively.

4 Borrowing

- 4.4 The Treasury Management Outturn Report for 2009/10 gave an overall outstanding Public Works Loan Board (PWLB) borrowing figure of £7.45m at an average interest rate of 4.73% and outstanding term remaining of 20 years at 31 March 2010.
- 4.5 Since that time, and in accordance with its borrowing strategy for 2010/11 the Authority has taken additional loans from the PWLB totalling £0.9m at an average interest rate of 4.44% and 24-year term. This rate is slightly more favourable than the target rate of 4.50% outlined in the annual strategy.
- 4.6 As a result, the Authority currently has a total of £8.35m PWLB loans at interest rates ranging between 3.97% and 5.875% and an average overall rate of 4.71%, and outstanding term remaining of 19 years.

5 Compliance with treasury management indicators

- 5.4 During the first six months of 2010/11, the Authority operated within the treasury management indicators set out in the Authority's Treasury Management Strategy.

Authorised limit for external debt

- 5.5 CIPFA's Code of Practice requires authorities to set an authorised limit for external debt, defined as the sum of external borrowing and other long-term liabilities. The annual strategy report presented to the Hampshire Fire & Rescue Authority on 10 February 2010 set an authorised limit of £25.6m.
- 5.6 This limit is based on the estimated Capital Financing Requirement (CFR) in order to enable it to be financed entirely from external borrowing should the Authority's internal reserves become depleted. The limit also includes an allowance for temporary borrowing to cover normal revenue cash flow requirements and unexpected outflows or delays in receiving cash.
- 5.7 During the 6-month period to 30 September 2010, the gross borrowing reached a maximum of £13.2m which is within the authorised limit of £25.6m.

Operational boundary for external debt

- 5.8 The Authority also needs to set an operational boundary for external debt. This should reflect the most likely scenario and be consistent with the Authority's capital plans and Treasury Management Strategy. Temporary breaches of the 2010/11 operational boundary can take place for cash flow reasons, but any sustained breach will lead to further investigation. The Authority approved an operational boundary for 2010/11 of £20.1m.
- 5.9 During the 6-month period to 30 September 2010, the gross borrowing reached a maximum of £13.2m which is within the operational boundary of £20.1m.

Upper limit on fixed interest rate exposure

- 5.10 The Authority has to set an upper limit on its fixed interest rate exposure, which is expressed in terms of the maximum long-term fixed-rate principal sums which can be outstanding on any day in each year. The Authority approved an upper limit on fixed interest rate exposure for 2010/11 of £10.1m.
- 5.11 During the 6-month period to 30 September 2010, the long-term fixed-rate principal sums outstanding reached a maximum of £8.35m which is within the upper limit on fixed interest rate exposure of £10.1m.

Upper limit on variable interest rate exposure

- 5.12 The Authority also has to set an upper limit on its variable interest rate exposure. This is calculated simply as the difference between the approved authorised borrowing limit and the fixed-rate borrowing outstanding at the end of each year if no further such borrowing is undertaken. The Authority approved an upper limit on variable interest rate exposure for 2010/11 of £15.5m.
- 5.13 During the 6-month period to 30 September 2010, the variable interest rate exposure reached a maximum of £5.7m which is within the upper limit of £15.5m.

Upper and lower percentage limits on the maturity structure of long-term fixed-rate borrowing outstanding in 2010/11

5.14 The Code also requires the Authority to set upper and lower percentage limits on the maturity structure of its long-term fixed-rate borrowing during 2010/11. The following table shows the limits approved by the Authority. These have been set in order to allow maximum flexibility in managing the debt portfolio and are consistent with the existing portfolio.

	Upper limit (%)	Lower limit (%)	Actual (%)
Under 12 months	0	0	0
12 to 24 months	30	0	0
24 months to 5 years	30	0	0
5 years to 10 years	30	0	1
10 years and beyond	100	70	99

Upper limits on investments with maturities longer than one year

5.15 For 2010/11, the Authority sets an upper limit of nil on investments for periods longer than one year. During the 6-month period to 30 September 2010, the Authority has not made any investments for periods exceeding a year and has therefore adhered to this limit.

6 Recommendation

6.4 That the mid-year review of treasury management activities be approved for submission to the Hampshire Fire & Rescue Authority.