

FLINTSHIRE COUNTY COUNCIL

REPORT TO: **AUDIT COMMITTEE**

DATE: **WEDNESDAY, 26 MARCH 2014**

REPORT BY: **HEAD OF FINANCE**

SUBJECT: **TREASURY MANAGEMENT UPDATE 2013/14**

1.00 **PURPOSE OF REPORT**

1.01 To provide members with a quarterly update on matters relating to the Council's 2013/14 Treasury Management Strategy up to the end of February 2014.

2.00 **BACKGROUND**

2.01 The Council has nominated the Audit Committee to be responsible for ensuring effective scrutiny of the Treasury Management Strategy.

2.02 The Audit Committee has previously agreed to include Treasury Management as a standing item on each quarterly agenda to receive an update.

3.00 **CONSIDERATIONS**

Investments Update.

3.01 A schedule setting out the Council's investments as at 28th February 2014 is attached at Appendix A. It shows a total investment balance of £56.0m spread across 15 counterparties with average interest rates of 0.55%.

3.02 As reported in the 29th January 2014 update the Council is gradually reducing the level of investments with the building society sector. This managed reduction can be seen when comparing the total invested with the sector at the end of December 2013 (£14.9m) to the total as at 28th February (£8.8m). Investments with most building societies are not being re-invested when they mature. New investments are being made mainly with other Local Authorities and Money Market Funds which are, in general, at a lower rate of interest.

Landsbanki

3.03 On the 3rd February 2014, the Council sold its claims against the insolvent estate of LBI (Landsbanki). All Members were notified of the sale by letter on 4th February 2014.

- 3.04 The claims were sold through a competitive auction process. The price at which the claims were sold was based on a reserve price set by the Council on the basis of legal advice received from Bevan Brittan, financial advice procured by the Local Government Association (LGA) and our own analysis of the financial position.
- 3.05 A number of other priority creditors/UK local authorities sold their claims through the same auction process. Each creditor who participated in that process achieved exactly the same auction price.
- 3.06 Members will be aware that the Council had £3.7m invested with LBI when the bank became insolvent in 2008, and that £1.947m had already been returned. The proceeds of the sale were paid in cash in Pounds Sterling and the sale means that the Council recovered 92% of the amounts that were originally deposited, representing a very large portion of the LBI deposits.
- 3.07 The sale of the claims represents a clean break and with the administration of the insolvent estate of LBI likely to continue for several years, removes the uncertainty around the timing of future recoveries. Future distributions could have been made in a number of currencies, including Icelandic Krona, which would have been less advantageous to the Council. As a result of the sale of the claims the Council is now no longer a creditor of LBI.
- 3.08 In order to maximise the position of those creditors taking part in the auction, the arrangements were made, with advice as set out in 3.04 above, by the Head of Finance and the Monitoring Officer. The sale of the claims was undertaken under delegated powers by the Head of Finance under Financial Procedure Rule 9.5, which is to agree the arrangements for the collection of all income due to the Council.

Borrowing Update

- 3.09 Officers, in conjunction with Arlingclose, continue to review and assess any debt restructuring or repayment options that may arise.
- 3.10 Attached at Appendix B is the schedule of all loans that the Council currently owes, amended to incorporate changes agreed at the Audit Committee on 29th January 2014. The schedule is categorised by the loan provider (either PWLB or market) and the interest type (either fixed or variable). The schedule shows per loan the:
- Start Date
 - Principal Outstanding
 - Interest Rate
 - Annual Interest Paid
 - Maturity Date

3.11 Loans marked with an asterisk have been taken out as a result of debt restructuring, where loans are repaid early and replaced with new loans either;

- To ensure that the number of loans the Council has are widely spread in terms of maturity, thus preventing an excessive number of loans needing to be repaid or refinanced in any one year when rates could be high. The debt maturity profile graph included in Treasury Management reports demonstrates Flintshire's appropriately spread loan portfolio.

Or

- To save interest costs by replacing higher rated loans with new loans at lower rates when the premium charged is not prohibitive.

3.12 As previously reported the schedule shows that the rates of interest charged on some loans are high by today's standards, however these loans were taken out at a time when those interest rates were the best available, and current interest rates remain at an all time low. At the Member training session on 27th January 2014, a detailed example of debt restructuring was worked through. Current opportunities for debt restructuring were discussed at the Audit Committee meeting on 29th January 2014. The Committee was satisfied that current premia charged are prohibitive and that processes are in place to review debt and to take debt rescheduling opportunities when appropriate.

LOBOs (Lender's Option Borrower's Option)

3.13 At the January Audit Committee meeting enquiries were made regarding the Council's LOBOs.

3.14 LOBO (Lender's Option, Borrower's Option) loans offer an initial fixed rate period and then enter a period of variable interest for the remainder of the loan. The interest rate is subject to review every 6 months. At this time only, the Lender can insist on a rate change (up or down) and the Council then has the option to accept the new rate or repay the loan.

3.15 Details of the Council's LOBOs are shown in the table below:

	Amount £m	Interest Rate	Start Date	Initial Fixed Period	End date	Annual Interest £
	6.35	4.48%	24.07.07	1 year	24.01.40	284,480
	6.30	4.53%	24.07.07	16 months	24.01.41	285,075
	6.30	4.58%	24.07.07	23 months	24.01.42	288,540
TOTAL	18.95					858,095

3.16 To date, the lender has not exercised their right to change the interest rates; it was able to do so for the first loan in the table above from July 2008. The interest rates are comparable with 25 year fixed rate PWLB loans (4.48% at the time of writing this report). At present the lender will not enter into negotiation regarding the possibility of early repayment, the situation is being monitored by Officers in conjunction with Arlingclose.

3.17 The query at the January Committee in particular asked what process would be followed were the lender to increase interest rates by a modest 25 basis points (bps) (0.25%) or to a much higher rate of 10%. For the 2 scenarios arising:

1. Increase of 25 bps – this would increase annual interest by £47,375 to £905,470.
2. Increase to 10% – this would increase annual interest by £1.037m to £1.895m.

In both instances, the Council would have the option to:

- continue with the loan thus paying the higher rate of interest
- repay the loan, either from reserves or by further borrowing.

In deciding which option to take the considerations would be similar to those when considering debt restructuring, which Members will be familiar with from the training on the 27th January 2014, including:

- Affordability from a budget perspective. The Council will suffer an increase in the amount of interest it has to pay.
- Affordability from a treasury perspective. The Council may or may not have sufficient cash available to repay the loan in full when needed.
- Interest rates on borrowing from other sources at the time.
- The Council's future plans for the use of reserves held and the capital programme.

3.18 Economic Context – provided by Arlingclose Ltd.

The outlook for growth in the Bank of England's Monetary Policy Committee's (MPC) February Inflation Report is stronger than that presented in November. The UK recovery has gained momentum and inflation has returned to the 2% target. Reduced uncertainty, easier credit conditions and loose monetary policy should support continued economic growth.

The headline unemployment rate is likely to reach the MPC's 7% threshold by the spring of this year. Even so, the Committee judges that there remains spare capacity, concentrated in the labour market.

Inflation is likely to remain close to the target over the forecast period. Given this, and with spare capacity remaining, the MPC judges that there remains scope to absorb slack further before raising Bank Rate.

Arlingclose's outlook for rates: Despite unemployment falling much more quickly than expected towards the threshold rate of 7%, further improvement in growth prospects and a benign outlook for inflation, the MPC have made it clear that the Bank Rate will remain low for some time to come. We currently forecast the first rate rise in 2016.

2014/15 Treasury Management Strategy

- 3.19 The Council approved the Treasury Management Strategy 2014/15 on 18th February 2014.

4.00 RECOMMENDATIONS

- 4.01 That Members note the report.

5.00 FINANCIAL IMPLICATIONS

- 5.01 None directly as a result of this report.

6.00 ANTI POVERTY IMPACT

- 6.01 None directly as a result of this report.

7.00 ENVIRONMENTAL IMPACT

- 7.01 None directly as a result of this report.

8.00 EQUALITIES IMPACT

- 8.01 None directly as a result of this report.

9.00 PERSONNEL IMPLICATIONS

- 9.01 None directly as a result of this report.

10.00 CONSULTATION REQUIRED

- 10.01 Arlingclose Limited.

11.00 CONSULTATION UNDERTAKEN

- 11.01 Arlingclose Limited.

12.00 APPENDICES

Appendix A – Investments Outstanding as at 28th February, 2014.
Appendix B – Schedule of Debt as at 28th February 2014

LOCAL GOVERNMENT (ACCESS TO INFORMATION ACT) 1985 **BACKGROUND DOCUMENTS**

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