Coventry City Council

Briefing note

To **Finance and Corporate Services Scrutiny Board 1**

Date 11th November

Subject **Treasury Management**

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1 Purpose of the Note

1.1 This item has been included on the Scrutiny Board work programme with the aim of looking at the Council's treasury management activity including cash balances and approaches to borrowing.

2 Recommendations

2.1 Scrutiny Board 1 is requested to consider the contents of the note.

3 Information/Background

3.1 This note gives an outline of the Council's Treasury Management (TM) activity which the Council undertakes as a fundamental part of its financial activities. TM activity involves managing the Council's cash-flow, ensuring that it has sufficient cash to fund its expenditure. This is achieved through a combination of borrowing and investing. In recent years, the Council's activity has been confined largely to long-term borrowing and short-term investments.

Long-Term Activity – Borrowing

3.2 Long-Term borrowing is undertaken to ensure that the Council can finance its capital expenditure and is dictated largely by the extent to which it needs to borrow to do this. The Council's underlying need to borrow is calculated after taking into account other resources available to fund the Capital Programme (for example, capital receipts).

3.3 The Council's borrowing requirement at 31st March 2015 was £292m, made up from the following sources:

Source of Borrowing	£m
Public Works Loan Board	221
Market Loans	59
Stock Issue	12

Total	**292**

3.4 The Public Works Loan Board **(PWLB)** is an agency of HM Treasury. The PWLB's function is to lend money to local authorities. The Council has a portfolio of loans that have been taken out over a number of years and are made on fixed rates. The average interest rate of these loans is 4.65% and the average duration until they need to be repaid is 27 years. If the Council were to repay any of these loans early in an effort to replace them with loans at lower rates it would be required to pay a premium. It is very rare for this premium to be sufficiently low to make early repayment worthwhile.

3.5 The Council's market loans have been taken out with banks and other financial institutions. The majority of these (£58m) are Lender Option, Borrower Option (LOBO) loans. LOBOs are a form of borrowing for which the lender has options to change the interest rate or to call-in the loans at specific points during the loan-term. These loans have a final maturity period (assuming no call-in) of between 39 and 62 years. There are three loan tranches operating at interest rates of between 3.90% and 4.75%. Some media reports this year have questioned whether these loans represent good value for money for local authorities. However, Coventry's interest rates are very much "in the pack" compared with the Council's other long-term loans and represent what we would consider to be reasonable rates in the context of local authority long-term borrowing. If any of the LOBOs were called by the lenders or if a higher rate was set by the banks, the Council could replace them with borrowing at broadly equivalent rates, potentially on the beneficial side depending on the term and the individual LOBO.

3.6 The Council's remaining £12m stock issue has a further 10 years to run and has an interest rate of 8.25% although it is important to consider this in the context of the prevailing interest environment. When the stock issue was taken out it was at a time when interest rates, including PWLB were much higher than they are now. The loan stock would have been taken out at a rate that was consistent with other rates available. A further factor was that Council borrowing was subject to more restrictions at that time and there were PWLB lending quotas for instance. This borrowing can sometimes be re-financed when market circumstances and those of the lender are favourable and this is reviewed periodically basis.

3.7 In recent years the Council has undertaken very little short-term borrowing. This occurs only when the Council has a very short-term cash-flow issue. The pattern of the Council's receipts and income (e.g. grant income) compared with its spending patterns (e.g. capital spending) has meant that it has been cash-rich over recent years, thus avoiding the need to borrow. This cash-rich position applies solely to the Council's treasury position, not its ability to fund its long-term budget.

Short-Term Activity - Investment

3.8 The Council undertakes temporary investment on a regular basis. Investments are made in line with the Council's Lending List – a list of those banking and government institutions that the Council's Investment Strategy allows us to invest cash balances with. The list is maintained in line with advice provided by our Treasury Management advisors (Arlingclose) which bases its judgement on information from credit rating agencies. This area of activity is monitored on a regular bases by the Audit and Procurement Committee.

3.9 The level of investment balances reported to the Audit & Procurement Committee in August stood at £150.7m. The breakdown of these balances is shown below.

	£m
Bank Deposits	80.9
Local Authority Deposits	0.0
Money Market Funds	24.3
Long Term Investments	23.7
Corporate Bonds	21.8
Total	**150.7**

3.10 Further description of the types of investment are provided below.

Bank deposits include: Temporary Loan Out (Deposit) – These are investments with a counterparty where the start date, maturity date, principal & interest rate is all agreed in advance and cannot be changed until maturity; Temporary Loan Out (Call Deposits) – These are investments with banks whereby the money is held by the bank for an indefinite amount of time until the Council chooses to have the money back with different accounts operating different notice periods, the longer the notice period, the higher the interest rate; Certificate of Deposit – These are similar investments to Temporary Loan Out (Deposits). However, there is a secondary market for them, meaning they can be sold before the maturity date for a profit or loss. This makes them more liquid.

Local Authority Deposits are investments between Councils where the start date, maturity rate, principal and interest rates are all agreed in advance.

Money Market Fund (MMF) Deposits – Funds whereby the authorities money is managed by an external fund manager. The Council invests in the fund along with several other organisations and money is pooled together & invested in a number of different counterparties. As the investments made by the fund manager vary daily, the rate of interest fluctuates daily. Money can be paid into and withdrawn instantly from these accounts & so they are used to manage the Council's day to day cash-flow.

Long-Term Investments include: Collective Investment Funds – Similar to MMF Deposits, these are investments whereby we give our money to a fund manager and they pool our money with other organisations to make investments on our behalf. The rate of interest is higher on these and tends to fluctuate more. As such these need to be viewed as long term investments in order to smooth out peaks & troughs, even though the Council can withdraw from these accounts with only a week's notice if required; Investment in a property portfolio - The rate of return tends to be higher on these investments but tend to fluctuate more and as such need to be viewed as long term investments in order to smooth out peaks and troughs. The Council can withdraw from these accounts at short notice if required.

Fixed (Corporate) Bonds – These are similar to Certificates of deposit in that maturity date and interest rates are agreed in advance & there is a secondary market to sell them if required. However, whereas Certificates of Deposits are with banks, Fixed Bonds can be taken out with banks and private companies.

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