

## Treasury Management

**Recommendation:**

That the treasury management performance for the period 1 April 2009 to 31 July 2009 be noted.

### **1 Summary**

Treasury Management performance for the last 4 months reflects the difficult market conditions that have prevailed over this period. Interest receipts are below the budget target and there is uncertainty with regard to the cost of borrowing. Some savings from borrowing may be available to offset the potential income shortfall forecast because of lower interest rates but this will be dependent on the borrowing strategy adopted.

### **2. Interest Receipts**

The Treasury Management Strategy places security above yield when considering investments. For this reason, when the ratings agencies and other commentators raised concerns about a number of UK building societies, all building societies were temporarily suspended from the Police Authority's counter party list. This has had an impact on returns for the first four months of the year, as short-term investments have been placed with the Debt Management Office (central government) and the returns are below market rates. In addition, base rates fell by a further 0.5% after the interest receipts budget was set in February. The combined impact of changes to the lending list and lower base rates is that forecast receipts for 2009/10 are £139,000 below the original target. It is possible that this will be made good in the remainder of the year.

### **3.0 Performance of the External Investment Manager**

The target return for the investment fund manager was set at 2.0%. The subsequent cut in base rates means that the latest annual forecast return is 1.75%. The return to 31 July is 0.54%. This is well above the benchmark of 0.18% which is based on the 7 day LIBID (London Interbank Bid Rate).

### **4.0 Performance of the Devon and Cornwall Investment Fund**

4.1 The Devon and Cornwall Police Investment Fund managed in house has continued to perform well with returns around 4% when the base rate is 0.5%. This is well ahead of the external manager and substantially ahead of the market. This is because of the deliberate strategy to make a number of long-term investments in 2008/9 when rates were good.

## **5.0 Borrowing**

- 5.1 The Capital Programme and Treasury Management Strategy included planned borrowing of £12m for the 2009/10. As usual, slippage on the capital programme means it may not be necessary to borrow to this level to fund the planned expenditure. It may, however, be useful in the context of the overall medium term financial strategy to maintain the planned level of borrowing to some degree so minimising the level of reserves used for financing capital expenditure.
- 5.2 Long-term borrowing rates are significantly above short-term lending rates and also above the target rate set in the budget. Long-term rates have not fallen in the same way as short-term rates - this is a product of the action taken by the government to manage the national economic situation. Furthermore long-term rates are forecast to increase over the medium term.
- 5.3 The current strategy with regard to borrowing is to borrow the minimum required to maintain overall cash balances at an appropriate level and to fund the remainder from cash balances (internal borrowing). A new loan of £2.0m was arranged on 7 August for 5 years at 3.19%. This will meet the minimum requirement. The interest rate is slightly above the target rate of 3.0%. The forecast contained in Annex 1 reflects this strategy.

## **6.0 Risk Management and Investment Activity**

- 6.1 In February, the Police Authority approved a counter party list consisting of named UK banks and building societies, local authorities and the Debt Management Office (central government). Overseas banks were suspended.
- 6.2 In May, all building societies were suspended from the counter party list following a downgrading of a number of societies by Fitch. In July the Nationwide Building Society was added back to the list. In addition, the Abbey National and the Alliance and Leicester were added to the list of UK clearing banks. These two banks are owned by the Spanish parent bank Santander. The revised counter party list is attached as Annex 2.
- 6.3 On the 1 July, the Police Authority received the expected £18.0m from the Home Office for pension top up grant. The majority of this funding will not be required in cash-flow terms until later in the year. New loans were arranged with the Nationwide Building Society and the Alliance Leicester for a total of £4.0m. In addition, a further £5.0m was placed with the Police Authority's external fund managers Investec. These loans are not included in the Devon and Cornwall Police Investment Fund.

## **7.0 Foreign Currency Transactions**

- 7.1 At the June meeting of Resources committee it was reported that:
- the major part of the purchase cost of the helicopter was due to be paid in July
  - the price for the new helicopter is fixed in the currency of manufacture (the airframe in euros and the role equipment in pounds, euros and US dollars)

In June it was unclear what the final sterling price would be as this would be dependent on movements in exchange rates between the date of the meeting and the date when the helicopter was delivered to the UK in July. The range of costs set out was a prudent forecast based on the relatively poor performance of the pound in the first four months of 2009.

Improvements in the strength of the pound in May continued throughout June and early July. For this reason the forecast increase in cost has not occurred. The final cost of the helicopter will be dependent on the exchange rates prevailing when the retention payments are made in January 2010 and January 2011. Based on current exchange rates it is unlikely that the final costs will be more than £6.9m as compared to the budget provision of £6.8m and the range up to £7.5m agreed by members.

## **8.0 Bank Contract**

Under the contract with Barclays Bank, the Police Authority has an overdraft facility that is negotiated annually. For 2008/9 the overdraft limit was £5.0m and there was no fixed fee. As result of recent changes in the banking markets Barclays Bank proposed an annual fee for 2009/10. As a result of negotiations with the bank it has been agreed to reduce the overdraft facility to £1.0m. The Treasurer will comment at the meeting.

## **9.0 Conclusion**

- 9.1 Market conditions are very challenging in terms of executing a successful Treasury Management Strategy. The bank base rate is at an all time low (0.5%) and market rates are still declining – this is limiting the return on cash-low balances for the present. Long-term rates on the other hand are rising with the potential to increase borrowing costs in the medium to long-term.

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## Annex 1

<b>Overall Performance and Budgetary Impact</b>			
	Revised Budget £000	Latest Forecast £000	Variance £000
Interest receipts	(1,139)	-1000	139
Cost of Borrowing for Capital Investment	1,207	1040	(167)
<b>Total Capital Financing</b>	<b>68</b>	<b>40</b>	<b>-28</b>

<b>Performance Against Benchmark</b>			
Period 1 April 2009 to 31 July 2009 % return on investment after fees			
	Benchmark %	Actual %	Difference %
Investec	0.18	0.54	0.36
Devon and Cornwall Police Investment Fund	0.18	1.70	1.52

<b>Forecast Return on Investment for Period 1 April 2008 to 31 March 2009</b>	
	Rate of Return %
Investec	1.75
Devon and Cornwall Police Investment Fund	4.00

## DEVON AND CORNWALL POLICE AUTHORITY

## Approved List of Borrowers

Revision No.21

8 July 2009

	D&C PA Counterparty £ millions	Lending Limits Group Limit £ millions
<b>1. UK CLEARING BANKS &amp; SUBSIDIARIES (GROUP LIMIT £)</b>		
BARCLAYS BANK	3	
BANCO SANTANDER CENTRAL HISPANO	3 }	3
ABBNEY NATIONAL	3 }	
ALLIANCE & LEICESTER	3 }	
HSBC BANK	3	
LLOYDS BANKING GROUP	3 }	3
BANK OF SCOTLAND	3 }	
LLOYDS TSB	3 }	
ROYAL BANK OF SCOTLAND	3 }	
<b>2. BUILDING SOCIETIES</b>		
NATIONWIDE	3 }	3
DUNFERMLINE (No further new deposits)	1 }	
BRITANNIA	SUSPENDED	1
CHELSEA	SUSPENDED	1
COVENTRY	SUSPENDED	1
LEEDS	SUSPENDED	1
NEWCASTLE	SUSPENDED	1
NORWICH & PETERBOROUGH	SUSPENDED	1
PRINCIPALITY	SUSPENDED	1
SKIPTON	SUSPENDED	1
WEST BROMWICH	SUSPENDED	1
YORKSHIRE	SUSPENDED	1
CUMBERLAND	SUSPENDED	1
KENT RELIANCE	SUSPENDED	1
NATIONAL COUNTIES	SUSPENDED	1
NOTTINGHAM	SUSPENDED	1
PROGRESSIVE	SUSPENDED	1
STROUD & SWINDON	SUSPENDED	1
<b>3. OVERSEAS BANKS ( &amp; SUBSIDIARIES ) OPERATING IN LONDON</b>		
ALLIED IRISH BANKS	SUSPENDED	3
BANK OF IRELAND	SUSPENDED	3
<b>4. LOCAL AUTHORITIES</b>		
COUNTY COUNCILS		3
METROPOLITAN AUTHORITIES		3
LONDON BOROUGHS		3
ENGLISH UNITARIES		3
SCOTTISH UNITARIES		3
DISTRICT COUNCILS		1
OTHER AUTHORITIES (eg. Police, Fire, etc.)		1
<b>5. DEBT MANAGEMENT ACCOUNT (CENTRAL GOVERNMENT)</b>		
DMA Deposit Facility (DMADF)		25



Devon and Cornwall Investment Fund Holdings									
	Start Date	Maturity Date	Length	Rate (%)	01-Jul-09	Forecast 01-Oct-09	Forecast 01-Dec-09	Forecast 01-Mar-10	Forecast 01-Jul-10
					£000	£000		£000	£000
Coventry Building Society	22/10/2007	01/10/2009	2 years	6.12%	2500	0	0	0	0
Principality Building Society	21/01/2008	01/03/2010	25 mths	5.15%	3000	3000	3000	0	0
Chelsea Building Society	21/01/2008	01/03/2010	25 mths	5.15%	1000	1000	1000	0	0
West Bromwich Building Soc	01/02/2008	01/03/2010	25 mths	5.10%	1000	1000	1000	0	0
Newcastle Building Society	27/06/2008	01/07/2010	2 years	6.73%	2500	2500	2500	2500	0
National Counties Building Society	16/03/2009	01/12/2009	8.5 mths	2.50%	1000	1000	0	0	0
Dunfermline Building Society	16/03/2009	01/12/2009	8.5 mths	2.50%	1000	1000	0	0	0
Nottingham Building Society	16/03/2009	01/12/2009	8.5 mths	2.45%	1000	1000	0	0	0
Norwich & Peterborough Building Society	17/03/2009	01/12/2009	8.5 mths	2.42%	1000	1000	0	0	0
Stroud & Swindon Building Society	17/03/2009	01/12/2009	8.5 mths	2.35%	500	500	0	0	0
<b>Total</b>					<b>14500</b>	<b>12000</b>	<b>7500</b>	<b>2500</b>	<b>0</b>