

**POLICY & RESOURCES CABINET BOARD**

**27<sup>th</sup> August 2009**

**FINANCE & CORPORATE SERVICES**

**REPORT OF THE HEAD OF FINANCIAL SERVICES  
– H. JENKINS**

**INDEX OF REPORT ITEMS**

**PART 1 - Doc.Code: PRB-270809-REP-FS-HJ**

<b>SECTION A – MATTERS FOR DECISION</b>		
<b>Report Item</b>	<b>Page Nos</b>	<b>Wards Affected</b>
1. Welsh Purchasing Consortium Energy Management	2 – 11	All
<b>SECTION B – MATTERS FOR INFORMATION</b>		
<b>Report Item</b>	<b>Page Nos</b>	<b>Wards Affected</b>
2. Annual Treasury Report 2008/09 and Amended Prudential Indicators for 2009/10 onwards	12 – 30	All
3. Insurance Renewals	31	All
4. Treasury Management	32 – 34	All

## **SECTION A – MATTERS FOR DECISION**

### **ITEM 1**

#### **ENERGY MANAGEMENT CONTRACT – WELSH PURCHASING CONSORTIUM**

##### **1. Purpose of Report**

This report sets out Energy Management work carried out by the Welsh Purchasing Consortium which was reported to Committee at the end of July 2009.

##### **2. Background**

2.1 Neath Port Talbot Council has previously entered into joint purchasing contracts for Energy, initially via purchasing arrangements led by City & County of Swansea and Newport Councils as lead authorities within the Welsh Purchasing Consortium and more recently the WPC has procured via the Office of Government Commerce Buying Solutions Contract.

2.2 This later contract expires on 31<sup>st</sup> October 2009.

##### **3. Welsh Purchasing Committee Proposals**

3.1 The WPC considered several options for the Energy Management arrangements. The attached report at Appendix 1 sets out the proposals and officers recommendation to the Board meeting of July 2009.

It was agreed that:

3.1.1. The methodology utilised for this review be noted.

3.1.2. The WPC seek to extend its arrangement with the Office of Government Commerce Buying Solutions (OGCBS) for a period of 3 years with an option to further extend for a period of up to 12 months thereafter.

3.1.3. Delegate the authority for the Welsh Purchasing Consortium to negotiate a new Service Level Agreement with the OGCBS that will delivery optimum performance and value for money, for all WPC members.

3.1.4. When the extended SLA expires the WPC seeks proposals from both the public and private sectors.

3.1.5. The WPC look to review its method of procuring energy again in January 2012.

3.2 Members will note the deliberations and work carried out together with the indicative best practice emanating from Central Government that the public sector should ensure they

- Maximise benefits from collaborative tendering.
- They must buy energy from the Wholesale Market thus using flexible, experienced managers to purchase energy.

A number of organisations meet the purchasing tendering criteria. Having reviewed these organisations, the Welsh Purchasing Consortium evaluated that the best outcome was to remain with OGCBS for a further 3 years but giving the authority to negotiate contract savings based on the WPC Purchasing Power.

3.3 The energy wholesale market, as previously reported to Members, is very volatile and significant price fluctuations are experienced not only due to UK supply/demand issues but also due to increased world demand from India/China, unrest in the Middle East, disruptions (or potential disruptions) to pipelines from Russia to Europe and UK, fluctuation in oil prices, severe weather predictions etc. All purchases made by Buying Solutions are made in the period 6 months prior to the contract year. The majority of this Council's Gas and Electricity (for properties consuming less than 2500 therms – Gas, 100kw - Electricity therms) have their contract year commencing in October, whilst larger properties, Electricity and Street Lighting contracts run annually from April.

3.4 For contract renewing in October 2009 it is anticipated that gas and electricity savings of circa 30% on October 2008 can be expected. This is against price increases of 60% and 90%+ last October.

## **Appendix**

Appendix 1 – Welsh Purchasing Consortium Energy Management Report July 2009.

#### **4. Recommendations**

- 4.1 that Members endorse the work of the Welsh Purchasing Consortium, continue to be part of the Energy Contract with Office of Government Commerce Buying Solutions and agree to the recommendations approved by the WPC Board at its July meeting as outlined in paragraph 3.1.

#### **Reason for Proposed Decision**

To comply with the Council's contract procedure rules and EU procurement directives.

#### **List of Background Papers**

Energy Management Site

#### **Wards Affected**

All

#### **Officer Contact**

Mr Hywel Jenkins – Head of Financial Services

Tel. No.: 01639 763646

E-mail: [h.jenkins@npt.gov.uk](mailto:h.jenkins@npt.gov.uk)

Mr Robert Type – Corporate Procurement Manager

Tel. No.: 01639 763034

E-mail: [r.type@npt.gov.uk](mailto:r.type@npt.gov.uk)

## COMPLIANCE STATEMENT

### ENERGY MANAGEMENT CONTRACT – WELSH PURCHASING CONSORTIUM

#### Implementation of Decision

The decision is proposed for implementation after the three day call in period.

#### Sustainability Appraisal

##### Community Plan Impacts

Economic Prosperity	-	Positive
Education & Lifelong Learning	-	Positive
Better Health and Well Being	-	Positive
Environment and Transport	-	Positive
Crime and Disorder	-	Positive

##### Other Impacts

Welsh Language	-	No Impact
Sustainable Development	-	Positive
Equalities	-	Positive
Social Inclusion	-	No Impact

#### Consultation

There has been no requirement under the Constitution for external consultation on this item.

**REPORT TO WELSH PURCHASING CONSORTIUM**

**SUBJECT: PROCUREMENT OF ENERGY**

**AUTHOR: CHAIR WPC ENERGY TASK AND FINISH GROUP 2009**

**1. PURPOSE OF THE REPORT**

- 1.1. To update WPC Management Board of the recent task and finish group set up to review, and recommend how the WPC should procure its' energy post October 2009 [this is the expiry date of the current WPC arrangement with buying solutions].

**2. RECOMMENDATIONS**

- 2.1. It is recommended that the WPC Management Board:-
  - 2.1.1.1. Note the methodology utilised for this review.
  - 2.1.1.2. Endorse the recommendation, that the WPC seek to extend its' arrangement with Buying Solutions (BS) for a period of 3 years with an option to further extend for a period of up to 12 months thereafter.
  - 2.1.1.3. Delegate the authority for RCT, in conjunction with the task and finish group chair to negotiate a new Service Level Agreement (SLA) with BS that will deliver optimum performance and value for money, for all WPC members.
- 2.2. That when the extended SLA expires the WPC seeks proposals from both the public and private sectors.
- 2.3. That the WPC look to review its' method of procuring energy again in January 2012.

### **3 BACKGROUND**

- 3.1 RCT provided an update to the WPC Management Board on 22<sup>nd</sup> April 2009, expressing a number of issues;
- The WPC Portfolio
  - BS Savings Model
  - BS Portfolio
  - Market Conditions
  - Out look
- 3.2 It was noted in the report that the current arrangement with BS expires on the 31<sup>st</sup> October 2009. It was verbally suggested at this meeting that a task and finish group be set up to appraise options available for the future procurement of energy for WPC members.
- 3.3 Following the WPC Management Board meeting in April a task & finish group was set up to;
- 3.4 Appraise options available to WPC members for the procurement of energy
- 3.5 Provide a report to WPC Management Board with recommendations for the future procurement of the WPC energy portfolio.

### **4 WPC STRATEGIC ENERGY REVIEW - TASK AND FINISH GROUP**

- 4.1 The task and finish group chair, in conjunction with RCT, and the WPC procurement manager discussed and agreed the resources needed to complete the task effectively.
- 4.2 It was agreed that a maximum of 15 and a combination of experienced; Procurement, Energy, and Street Lighting officers should be represented on the group. This ensured optimising a balance of expertise and experience in energy procurement be taken advantage of, for the completion of this task.
- 4.3 Appendix 1 details the task and finish group membership, and terms of reference.
- 4.4 An invitation to potential members [of the task & finish group] was well received and a meeting/workshop of the task and finish group convened on the 29<sup>th</sup> of May 2009.

## **5 TASK AND FINISH GROUP APPRAISAL, and METHODOLOGY**

- 5.1 The purpose of the workshop on the 29<sup>th</sup> May was to agree the terms of reference, and work through the appraisal methodology which is summarised below;
- 5.2 Undertake a SWOT analysis on 5 agreed potential energy buying scenarios;
- Status Quo – As is
  - BS Improved
  - WPC utilise its own resources to procure energy (Make or Buy)
  - Move to AN Other public sector partner via restricted competition
  - Move to a private sector partner via open competition
- 5.3 The results of the SWOT analysis will determine the potential options that should be explored see appendix2 [notes from workshop].

## **6 THE UK ENERGY STRATEGY TEAM**

- 6.1 Central Government have commissioned an Energy Strategy Team to look at how UK public sector organisations procure their energy. The team is governed by the Office of Government Commerce (Whitehall – separate from the BS team) and chaired by the Ministry of Defence MOD, representatives of the group include, NHS, ESPO, WAG, TEC etc....
- 6.2 The objective of the group is to endorse methods and performance of collaborative energy buying organisations, which carry out the buying of energy on behalf of other public sector organisations.
- 6.3 Each endorsed method is evaluated using robust criteria such as (in no particular order);
- Risk Management Strategy
  - Transparency and Integrity
  - Flexibility
  - Aggregation
  - Data Management
  - Contract Management
  - Administration Cost
  - Administration Methods
  - Performance Measurement
  - Benefits Analysis
  - Communication
  - Billing Stability
  - Supplier Management
  - Market Intelligence



- Future Strategies

6.4 The aim of the group is to signpost public sector organisations who carry out the buying [of energy] autonomously to endorsed organisations to enhance performance and value for money.

## 7 OUTCOME OF THE WPC STRATEGIC ENERGY REVIEW - TASK AND FINISH GROUP

7.1 The results of the SWOT analysis are as follows;

Scenario	Strengths / Opportunities	Weaknesses / Threats	Pursue?
Status Quo	17	11	No
OGC Improved	16	5	Yes
Seek Proposal From a Public Sector Partner	9	9	Yes
Seek Proposal From a Private Sector Partner	10	15	No
WPC Make or Buy	11	16	No

7.2 A lengthy debate took place during the workshop around the possibility of inviting a private sector partner to submit a proposal to procure the WPC energy portfolio. It was agreed that the WPC do not take this opportunity at this time due to the following reasons;

7.2.1 Timescales and resources needed to procure such a partner

7.2.2 Political acceptance i.e. the UK – EST at this present time

7.3 Therefore synonymous to the appraisal methodology the SWOT analysis suggested that the two scenarios the WPC should explore were;

7.3.1 Seek proposals from Public Sector Partners

7.3.2 Improve current SLA with BS

7.4 It was agreed that if the WPC were to seek proposals from Public Sector Partners the proposal should be evaluated using the criteria adopted by the UK - EST. It was also agreed that the request for proposals be restricted to organisations, that;

- 7.5 Are already endorsed by UK - EST
- 7.6 Such organisations satisfy two pass fail questions:
- 7.6.1 They must buy energy from the Wholesale market.
- 7.6.2 They must have at least double quantity of WPC portfolio going to market.
- 7.7 Approach to Endorsed UK - EST Organisations
- 7.8 The chair approached UK – EST endorsed organisations with a view to obtaining an appetite for each organisation to submit a proposal to procure the WPC energy portfolio. Such organisations were;
- LASER
  - WEST MERCIA
  - ESPO
  - NEPO
  - TEC
- 7.9 The only organisation which expressed an interest was ESPO. However ESPO were unsuccessful with the pass/fail criteria set by the task & finish group as their current energy buying power is £60m for 5000 sites, where as the WPC portfolio is £100m for 9000 sites. The pass fail threshold was at least double that of the WPC portfolio.
- 7.10 It was noted by the chair that UK – EST members aims were to target public sector organisations who procure energy autonomously, not compete with other members of the UK – EST group for selected portfolios.
- 7.11 RCT in conjunction with BS have recently been calculating the value of BS cost savings as a result of the collaborative tendering process adopted by BS. BS adopts a robust risk mitigating procurement strategy and have recently managed to negotiate capture and measure savings for WPC members. The savings are as follows;

<b>Authority</b>	<b>Savings</b>
Caerphilly	£173,950.00
Vale of Glamorgan	£115,662.00
Rhondda Cynon Taff	£234,247.00
Swansea	£253,622.00
Cardiff	£297,392.00
Blaenau Gwent	£117,434.00
Bridgend	£134,052.00
Neath Port Talbot	£168,806.00
Newport	£155,800.00
Monmouthshire	£82,994.00
Torfaen	£128,024.00
Merthyr Tydfil	£52,908.00
Pembrokeshire	£47,439.00
Carmarthenshire	£67,682.00
Powys	Nil – Only Just Transferred to BS
<b>Total</b>	<b>£2,030,012.00</b>

## 8 CONCLUSIONS

- 8.1 Should the WPC Management board endorse the recommendation to extend the current arrangement with BS, the delegated officers will ensure;
- 8.2 That delegated officers will utilise the UK – EST criteria to develop the existing performance framework between WPC and BS.
- 8.3 Utilise the Weaknesses and Threats identified in the (As is) status quo scenario to bolster the arrangement so that optimum performance and Value for Money is achieved.
- 8.4 Produce annual performance reports to the Management Board for information purposes.

**Report End**  
**WPC Strategic Energy Review Team**  
**July 2009**

**PART 1**  
**SECTION B – MATTERS FOR INFORMATION**

**ITEM 2**

**ANNUAL TREASURY REPORT 2008/09 AND AMENDED  
PRUDENTIAL INDICATORS 2009/10 ONWARDS**

**Introduction and Background**

The Chartered Institute of Public Finance and Accountancy's Code of Practice on Treasury Management 2001 was adopted by Council on 21<sup>st</sup> March 2002 for adoption from 1<sup>st</sup> April 2002, and this Authority fully complies with its requirements.

The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the Council of an annual treasury management strategy report (including the annual investment strategy report) for the year ahead and an annual review of the previous year.
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

Treasury management in this context is defined as:

*“The management of the local authority's 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”.*

## THIS ANNUAL TREASURY REPORT COVERS

1. The Council's treasury position as at 31<sup>st</sup> March 2009;
2. Performance measurement;
3. The strategy for 2008/09
4. The economy in 2008/09;
5. Borrowing and investment rates in 2008/09;
6. The borrowing outturn for 2008/09;
7. Compliance with treasury limits and Prudential Indicators;
8. Investment outturn for 2008/09;
9. Icelandic Bank Defaults;
10. Debt rescheduling;
11. Other issues

### 1. TREASURY POSITION AS AT 31 MARCH 2009

The Council's debt and investment position at the beginning and the end of the year was as follows:

	31st March 2009 Principal	Rate/ Return		31st March 2008 Principal	Rate / Return
<b>FIXED RATE FUNDING</b>					
- PWLB	£155.8m	5.5%		£157.1m	5.5%
- Market LOBOs	£62.5m	3.9%		£52.5m	3.9%
Variable Rate Funding:	£0	-		£0	-
<b>Total Debt</b>	<b>£218.3m</b>	<b>5.07%</b>		<b>£209.6m</b>	<b>5.17%</b>
<b>INVESTMENTS</b>					
<b>Total Investments</b>	<b>£93.2m</b>	<b>4.43%*</b>		<b>£77.2m</b>	<b>6.0%</b>

\*Excludes all interest from Icelandic Investment.

NB: **PWLB** = Public Works Loan Board which is a body the Government has established to lend money to Local Government  
**Market LOBO's** = Lender Option Borrower Option – this is borrowing from the market when the lender has offered a long term loan but with options to continue or foreclose on the loan at various specific intervals.

## **2. PERFORMANCE MEASUREMENT**

One of the key changes in the revision of the Code in 1996 was the formal introduction of performance measurement relating to investments, debt and capital financing activities. Whilst investment performance criteria have been well developed and universally accepted, debt performance indicators continue to be a more problematic area with the traditional average portfolio rate of interest acting as the main guide.

Section 6 and 8 of this report provides information against which annual performance can be measured.

## **3. THE STRATEGY FOR 2008/09**

The strategy approved by Council in April 2008 for 2008/09 was based upon the Authority's Adviser forecasts for new borrowing rates and investment interest rates as set out below:

- The 50 year PWLB rate is expected to fall marginally from 4.50% in Q1 2008 to 4.45% in Q2 2008 before rising back again to 4.50% in Q2 2009 to eventually reach 4.65% in Q2 2010.
- The 25 year PWLB rate is expected to fall from 4.55% to 4.50% in Q2 2008 and then to rise in gradual steps from Q2 2009 to reach 4.75% in Q3 2010.
- The 10 year PWLB rate is expected to fall from 4.60% in Q1 2008 to 4.55% in Q2 and to 4.30% in Q3 2008 and to then gradually rise from Q1 2009 to reach 4.85% in Q3 2010.
- The 5 year PWLB rate is expected to fall from 4.55% in Q2 2008 to 4.50% in Q3 2008 and to then gradually rise starting in Q1 2009 to reach 4.85% in Q2 2010.

This forecast suggests that there is a range of options available for the borrowing strategy in 2008/09. Variable rate borrowing is expected to be more expensive than long term borrowing and will therefore be unattractive throughout the financial year compared to taking fixed rate borrowing. There is expected to be little difference between 5 – 50 year PWLB rates which may provide opportunities for new borrowing to smooth the debt maturity profile away from a concentration in long dated debt. There is also expected to be little variation in rates during the year so borrowing could be undertaken at any time in the year.

In order to minimise debt interest costs, the main strategy proposed will therefore take account of these projections and in particular should PWLB interest rates fall back to 4.5%, then a new loan request will be taken out over the appropriate investment period.

Against this background caution will be adopted with the 2008/09 treasury operations. The Director of Finance will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to The Policy and Resources Board at the next available opportunity.

#### Sensitivity of the forecast

The main sensitivities of the forecast are likely to be the two scenarios below. The Authority officers, in conjunction with its treasury advisers, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- *if it were felt that there was a significant risk of a sharp rise in long and short term rates, perhaps arising from a greater than expected increase in world economic activity or further increases in inflation, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.*
- *if it were felt that there was a significant risk of a sharp fall in long and short term rates, due to e.g. growth rates weakening, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term funding will be considered.*

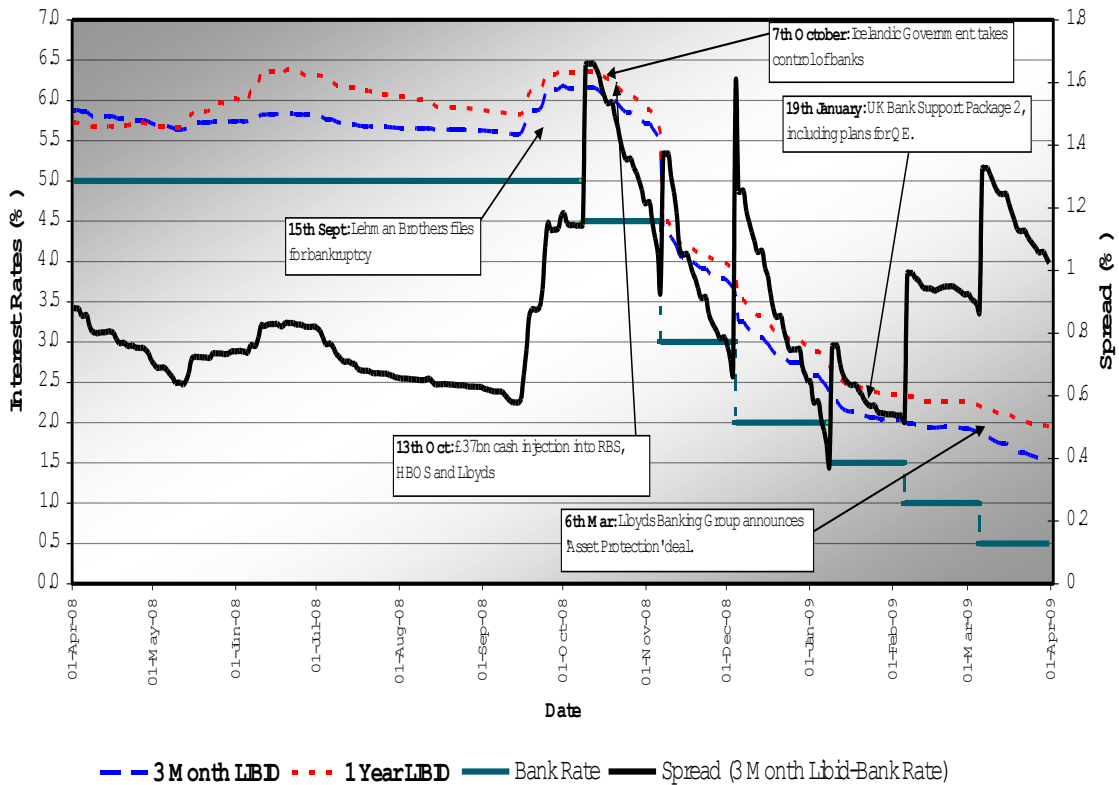
Market borrowing arranged during 2007/08 at favourable rates has reduced the necessity for additional external funding to finance capital expenditure in 2008/09. It may not be necessary to arrange additional borrowing during 2008/09, utilising surplus authority cash instead.

## **5. THE ECONOMY AND INTEREST RATES**

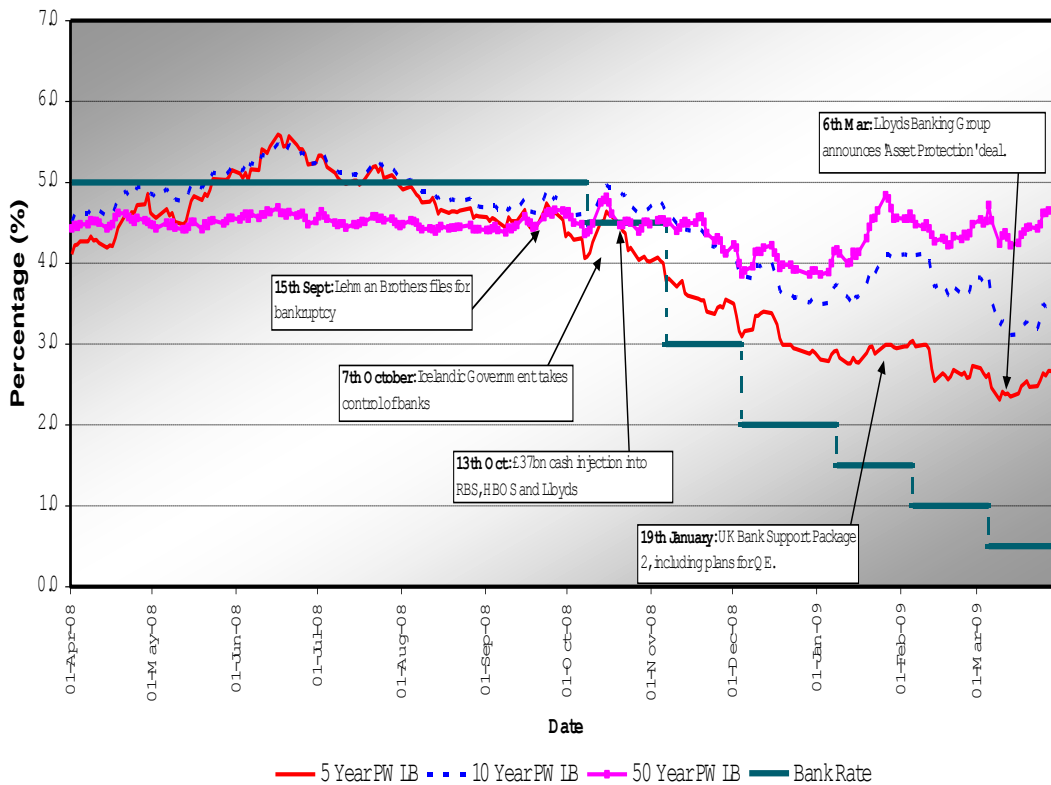
The financial turmoil in 2008/09 commonly known as the ‘credit crunch’ had a major downward impact on the levels of interest rates around the world. Although interest rates initially fell sharply in the US they were followed, eventually, by the Bank of England who aggressively cut Bank Rates.

The major economic events and interest rates during 2008/09 have been summarised on the following graph:

Bank Rate vs. Investment Rates 2008-09 and Spread Between 3 Month Libid & Bank Rate



PW LB Borrowing Rates vs. Bank Rate 2008-09



A summary of the major economic events during 2008/09 financial year:



## April 2008

At the beginning of 2008/09 financial year:

- UK Bank Rate was 5% and the Bank of England was focused on fighting inflation. Market fears were that rates were going to be raised as the Consumer Price Index (CPI), the Government's preferred inflation target, was well above the 2% target (two years ahead).
- The money market yield curve reflected these concerns with one year deposits trading well above the 6% level.
- PWLB rates in both 5 and 10 years edged above Bank Rate during the summer as markets maintained the belief that inflation was the major concern of the monetary authorities.
- The money markets were reflecting some concerns about liquidity at this time and, as shown in the graph, the spread between Bank Rate and 3 month London Interbank Offered Rate (LIBOR) was greater than had historically been the case.

## September 2008

- Lehman Brothers, a US investment bank, was allowed to file for bankruptcy in the total absence of any other institution being willing to buy it due to the perceived levels of toxic debt it had. This event caused a huge shock wave in world financial markets and threatened to completely de-stabilise them. As can be seen from the charts this also led to an immediate spike up in investment rates as markets grappled with the implications this might have on other financial institutions, their credit standing and indeed their viability.

## October 2008

- On 7th October the Icelandic Government took control of their banks and this was followed a few days later by the UK government pumping a massive £37bn into three UK clearing banks, Royal Bank of Scotland (RBS), Halifax Bank of Scotland (HBOS) and Lloyds, as liquidity in the markets dried up.

- The Monetary Policy Committee meantime had reduced interest rates by 50bp (basis points) on 9th October. This had little impact on 3 month LIBOR, however, as the spread, or ‘disconnect’ as it became known, against Bank Rate widened out. On the other hand the short end of the PWLB fell dramatically as investors, very concerned about their counterparty limits post the Icelandic banks’ collapse, fled to the quality of Government debt forcing yields lower.

### November 2008

- Market focus now shifted from inflation concerns to concerns about recession, depression and deflation. Although CPI was still well above target it was seen as no barrier to interest rates being cut further. The Monetary Policy Committee (MPC) duly delivered another cut in interest rates in November, this time by an unprecedented 1.5%. Investors continued to pour money into Government securities across the curve, at the front end because of credit concerns and the longer end because of the economic consequences reducing inflation, driving yields in 10 year PWLB temporarily below 4% and 5 years to around 3.5%.

### December 2008

- As the ramifications of the ‘credit crunch’ became increasingly clear the Bank of England cut interest rates to 2%-a drop this time of 1%. The whole interbank yield curve shifted downwards but the ‘disconnect’ at the short end remained very wide, negating to some degree the impact of the cuts in Bank Rate. 50 year PWLB rates dropped below 4% at the turn of the year, marking the low point, as it turned out, in this maturity.

### January 2009

- The New Year of 2009 brought little relief to the prevailing sense of crisis and on 8th January the MPC reduced rates by 0.5% to 1.5%, a record low. More Government support for the banking sector was announced on 19th January 2009. The debt markets had a sharp sell-off at this stage as they took fright at the amount of gilt issuance likely to be needed to finance the help provided to the banks. There was also discussion about further measures that could be introduced to kick start lending and economic activity. These included quantitative easing by the Bank of England, effectively printing money.

## February 2009

- the MPC adopted the traditional method of monetary easing by cutting interest rates again by 0.5% to 1%. Interbank rates drifted down with the spread in the 3 months still well above Bank Rate.

## March 2009

- Lloyds Banking Group, which now included HBOS, took part in the Government's Asset Protection scheme. The MPC cut interest rates yet again to 0.5% and announced the quantitative easing scheme would start soon. This scheme would focus on buying up to £75bn of gilts in the 5-25 year maturity periods and £10 -15bn of corporate bonds. This led to a substantial rally in the gilt market, particularly in the 5 and 10 year parts of the curve, and PWLB rates fell accordingly. Finally at the end of March it was announced that the Dunfermline Building Society had run into difficulties and its depositors and good mortgages were taken over by Nationwide whilst the Treasury took on its doubtful loans.

The financial year ended with markets still badly disrupted, the real economy suffering from a lack of credit, short to medium term interest rates at record lows and a great deal of uncertainty as to how or when recovery would take place. Investment income returns have been badly hit but lower borrowing rates in short to medium periods had allowed indebted local authorities to benefit.

## **6. BORROWING AND INVESTMENT RATES IN 2008/09**

### 12-month bid rates

One year London Inter Bank Bid Rate fluctuated between around 5.7% to 6.4% with two peaks driven by credit crunch fears in June and September. Bank Rate had been held at 5.0% until October 9 when the first of a series of major cuts caused 12 month LIBID in 2008-09 to be on a rapidly falling trend to the end of the financial year, reaching 1.85% at the end.

## Longer-term interest rates

The PWLB 45-50 year rate started the year at 4.43% and was then generally within a band of 4.3 - 4.6% until mid October when there was a spike up to 4.84% followed by a plunge down to 3.86% in early December. Further spikes of 4.84% and 4.72% occurred in late January and early February with the year closing out at 4.58%. It was not uncommon to see rates fluctuating by 40-50 basis points within a few weeks during this year.

## **7. BORROWING OUTTURN FOR 2008/09**

Actual borrowing undertaken during the year:

<b>DATE</b>	<b>LENDER</b>	<b>AMOUNT</b>	<b>RATE</b>	<b>PERIOD</b>	<b>DETAILS</b>
17 Sept 08	Dexia Public Bank	£10.0m	4.01%	70 yrs	- Initial 5yrs fixed to Sept 2013 -Maturity date 17 Sept 2078

Comparative borrowing performance indicators for 2008/09:

- average PWLB maturity loan interest rates

1 year	3.264%
9.5 - 10 year	4.477%
24.5 - 25 year	4.570%
49.5 - 50 year	4.438%

## Debt Performance

As highlighted in section 1 above the average debt portfolio interest rate has reduced over the course of the year from 5.17% in 2007/08 to 5.07% in 2008/09.

The approach adopted during the year up to October 2008 was to draw longer term fixed rate debt, to take advantage of low long term rates and reduce exposure to fluctuations in short term interest rates. After this date no new loans were entered into as investment returns fluctuated significantly and then towards the end of the financial year, fell away dramatically.

## **7. COMPLIANCE WITH TREASURY LIMITS**

During the financial year the Council operated within the treasury limits and Prudential Indicators set out in the Council's annual Treasury Strategy Statement. The outturn for the Prudential Indicators is shown in Appendix 1.

## **8. INVESTMENT OUTTURN FOR 2008/09**

### Internally Managed Investments

The Authority manages all its investments in-house and invests with institutions which satisfy the Authority's approved criteria.

The Authority usually invests for a range of periods from overnight to 364 days, although investments of up to 5 years are permitted. All investments are dependent on the Authority's cash flows, its interest rate view and the interest rates on offer.

### Investment Strategy

The short-term investment strategy for in-house managed funds was based upon the Authority's view was that the market's expectation for Bank Rate was too high, and investments were accordingly weighted to longer periods, with a view to enabling returns to be maintained in a falling interest rate environment.

### Change in strategy and credit policy during the year

The strategy and policies adopted in the Treasury Management Strategy Report and Annual Investment Strategy for 2008-09 approved by the Council on 4<sup>th</sup> March 2008, was subject to major revision during the year due to the unprecedented impact of the credit crunch on world economies and the world banking system which resulted in a rapid fall in central bank rates around the world during the year, including in the UK, and correspondingly in the Council's investment returns in the second half of the year.

In addition, the default of the Icelandic banks in October 2008 led to a major review of credit policy by this council. In order to reduce exposure to credit risk the duration of investments was restricted and the Fitch counterparty ratings reviewed. Investments were made only with the better F1 and F1+ short term rated institutions which also met other specified rating criteria. This action however is likely to have an adverse effect on future investment earnings returns.

### Alternative investment strategy

Throughout the 2008/09 financial year, market interest rates were determined by the continuing lack of liquidity in the market place with banks remaining uneasy about lending. Continuing fears about the credit crunch forced the level of all market rates higher than in normal times. Whilst adversely affecting borrowers, investors were the benefactors of these conditions, with deposit rates remaining inflated, enabling an element of core funds to be lent in the longer term to secure good returns over the course of the 12 months (with some maturing into 2009/10).

The collapse of Lehman's and the Icelandic banking system in September/October 2008 created an environment of fear, and the nationalisation and part nationalisation of many financial institutions was necessary to secure the global financial system in the face of hundreds of billions of pounds worth of toxic asset related losses. Governments commenced a series of stimulus packages aimed at kick starting the global economy and central banks, helped by a downturn in inflation and inflation expectations, and so began an aggressive policy of interest rate cuts which has seen interest rates, reducing to record low levels.

### Investment Outturn for 2008/09

Detailed below is the result of the investment strategy undertaken by the Council:

	<b>Average Investment</b>	<b>External Interest Earned</b>	<b>Rate of Return</b>	<b>Benchmark Return</b>
<b>All figures exclude Icelandic Investments</b>	£90.8m	£4.3m	4.74%	<b>4.49%</b>

Relevant benchmarks for 2008/09:

- LIBID

7 day LIBID un-compounded	3.69%
3 Month LIBID un-compounded	4.49%

- Bank rates during the year

01 Apr 08	5.25%
10 Apr 08	5.00%
8 Oct 08	4.50%
6 Nov 08	3.00%
04 Dec 08	2.00%
08 Jan 09	1.50%
05 Feb 09	1.00%
05 Mar 09 to date	<u>0.50%</u>
<b>Weighted Average 2008/09</b>	<b><u>3.61%</u></b>

The benchmark for internally managed funds is the 3 month LIBID rate un-compounded. This rate reflects a realistic neutral investment position for core investments with a medium term horizon and a rate which is more stable with fewer fluctuations caused by market liquidity. Historically, this rate has been slightly higher than the 7-day rate and therefore more challenging for the manager, but one which does not necessitate a significantly increased level of risk.

## 9. ICELANDIC BANK DEFAULTS

In October 2008 the Icelandic banking system collapsed and as Members are aware, at 31<sup>st</sup> March 2009 the authority had the following investments totalling £20m frozen in Icelandic banks or their UK subsidiaries:

<b>BANK</b>	<b>AMOUNT</b>
<b>GLITNIR BANK</b>	<b>£2.0m</b>
<b>HERITABLE BANK</b>	<b>£9.0m</b>
<b>KAUPTHING SINGER AND FREIDLANDER</b>	<b>£3.0m</b>
<b>LANDSBANKI ISLANDS HF</b>	<b>£6.0m</b>
<b>TOTAL</b>	<b>£20.0m</b>

The Icelandic Government has stated its intention to honour all its commitments as a result of their banks being placed into receivership. The U.K. Government is working with the Icelandic Government to help bring this about. At the current time it is not possible to say with certainty that we will recover the entirety of our investment(s) or when reimbursements will be made to this authority. The Local Government Association is coordinating the efforts of all UK authorities with Icelandic investments. Members will be periodically updated on the latest developments on these efforts.

The English Government, the National Assembly of Wales have issued regulations to allow local authorities to delay recognising any loss on these investments that may eventually be incurred until the financial year 2010-11.

#### Icelandic Banks Update

The first distribution to creditors was made in July 2009 by the Administrators of the Icelandic Banks UK subsidiaries Heritable and Kaupthing Singer and Friedlander. Payments totalling £2.1m have been received by the Authority, £1.5m in respect of Heritable Bank and £0.6m KSF.

## **10. DEBT RESCHEDULING**

The main way for making savings was therefore to consider the potential for moving from PWLB debt to LOBOs at lower rates. This did not prove to be viable as due to the credit crunch, the supply of LOBO finance generally dried up after September 2008.



After the Icelandic banks defaulted in October, the Council undertook a major review of its investing and borrowing strategies. In the light of the perceived increased risk of holding surplus cash as investments and the likely poor rate of return available on such investments, it was decided to run down cash balances by not undertaking new borrowing to finance capital expenditure.

In an attempt to reduce cash balances further, the possibility of prematurely repaying PWLB debt was also explored, however the penalties arising from the early repayment of debt proved prohibitive and was not pursued.

The PWLB introduced a new rate interest rate structure on 1<sup>st</sup> November 2007, which imposed two rates for each period, one for new borrowing and a new, significantly lower rate for early repayment of debt. Daily movements of 1bp instead of 5 bp and rates in half year periods throughout the maturity range (previously had been mainly in 5 year bands) were also introduced which effectively prevented the Council from restructuring the portfolio into new PWLB borrowing.

## **11. OTHER ISSUES**

The transfer of the housing stock remains on the Authorities agenda and is likely to have a significant effect on the Authorities treasury function. A ballot of the tenants is due later in this financial year.

## **Appendix 1: Prudential Indicators**

## **12. RECOMMENDATION**

It is recommended that members note the content of this report including Performance Indicator information.

**List of Background Papers**

Treasury Management Closing 2008/09

**Wards Affected**

All

**Officer Contact**

Mr Hywel Jenkins - Head of Financial Services

Tel No 01639 763646

E-mail: [h.jenkins@npt.gov.uk](mailto:h.jenkins@npt.gov.uk)

Mr Mark Davies – Chief Accountant (Corporate, Capital & Risk  
Management)

Tel No 01639 763602

E-mail: [m.davies4@npt.gov.uk](mailto:m.davies4@npt.gov.uk)

**PRUDENTIAL INDICATORS FOR PERIOD 2009**

**A1. Capital Expenditure Indicators**

A1.1 Estimates of Capital Expenditure

‘The local authority will make reasonable estimates of the total capital expenditure that it plans to incur during the forthcoming financial year and at least the following two financial years. The estimates below are based on the latest approved budgets which will be revised when changes to the capital programme are known.

	<b>2008/09 Revised £'000</b>	<b>2008/09 Actual £'000</b>	<b>2009/10 Estimate £'000</b>	<b>2010/11 Estimate £'000</b>	<b>2011/12 Estimate £'000</b>
General Fund	47,095	46,361	35,248	28,781	23,770
<i>HRA</i>	8,562	7,947	8,634	8,000	6,200
<b>TOTAL</b>	<b>55,657</b>	<b>54,308</b>	<b>43,882</b>	<b>36,781</b>	<b>29,970</b>

\* The Authority expects to supplement its Capital Expenditure Programme in 2009/10 and beyond through additional external grant funding of projects. These figures will be updated in future years.

A1.2 Estimates of Capital Financing Requirement

The term Capital Financing Requirement represents the projected total amount of borrowing needed to fund Capital Expenditure. The sums involved are shown below:

	<b>2008/09 Revised £'000</b>	<b>2008/09 Actual £'000</b>	<b>2009/10 Estimate £'000</b>	<b>2010/11 Estimate £'000</b>	<b>2011/12 Estimate £'000</b>
General Fund	178,768	179,252	185,447	195,006	202,436
<i>HRA</i>	36,156	36,506	35,218	33,956	32,719
<b>TOTAL</b>	<b>214,924</b>	<b>215,758</b>	<b>220,665</b>	<b>228,962</b>	<b>235,155</b>

\* It should be noted that the possible Landlord Stock Voluntary Transfer has been ignored in the above calculation but this will be taken into account once the result of the ballot is known.

**A2. External Debt Indicators****A2.1 Operational Boundary**

The local authority will set for the forthcoming financial year and the following two financial years an operational boundary for its total external debt. The operational boundary should be based on the Authority's estimate of most likely i.e. prudent, but not worst case scenario.

	<b>2008/09 Revised £'000</b>	<b>2008/09 Actual £'000</b>	<b>2009/10 Estimate £'000</b>	<b>2010/11 Estimate £'000</b>	<b>2011/12 Estimate £'000</b>
Operational Boundary	251,960	242,445	265,682	275,891	283,937

**A2.2 Authorised Limit**

The local authority will set for the forthcoming financial year and the following two financial years an authorised limit for its external debt.

	<b>2008/09 Revised £'000</b>	<b>2008/09 Actual £'000</b>	<b>2009/10 Estimate £'000</b>	<b>2010/11 Estimate £'000</b>	<b>2011/12 Estimate £'000</b>
Authorised Limit	271,960	262,445	285,682	295,891	303,937

**A3. Treasury Management Indicators**

The following Treasury Management Indicators are required:-

A3.1 The Council adopted the CIPFA Code of Practice for Treasury Management in the Public Services in 2002. This indicator reaffirms the Authority's commitment to comply with the Code of Practice.

A3.2 The following limits be established to administer interest rate exposure for the next 3 years.

	<b>2008/09</b>	<b>2009/10 to 2011/12</b>
	<b>Actual £'000</b>	<b>Estimate £'000</b>
<i>Upper Limit on Fixed Interest Rate Exposure</i>	145,489	213,937
<i>Lower Limit on Fixed Interest Rate Exposure</i>	0	0
Upper Limit on Variable Interest Rate Exposure	72,745	106,969
Lower Limit on Variable Interest rate Exposure	0	0

The above limits will be measured upon the net principal invested method. This method takes account of total borrowing outstanding less principal sums invested.

A3.3 The Borrowing Maturity structure will be:

	<b>Upper Limit %</b>	<b>Lower Limit %</b>	<b>2008/09 Actual %</b>
Under 12 months	15	0	4
12 months to 2 years	15	0	1
<i>2 to 5 years</i>	40	0	2
5 to 10 years	60	0	7
10 years +	100	15	86

**A4. Affordability Indicators**

These indicators consider the estimated impact of capital financing costs on the net budget, taxpayers and housing tenants of the Authority.

	<b>2008/09 Revised £'000</b>	<b>2008/09 Actual £'000</b>	<b>2009/10 Estimate £'000</b>	<b>2010/11 Estimate £'000</b>	<b>2011/12 Estimate £'000</b>
<b>Estimated ratio of financing cost to net revenue stream:</b>					
- for General Fund	7.18%	6.76%	6.77%	6.41%	6.32%
- for HRA	10.23%	10.47%	9.45%	8.14%	6.90%
<b>Estimate of incremental impact of new capital investment decisions on:</b>					
- Council Tax	NA	£24.53	£9.62	-£7.69	£4.04
- Housing	0	0	0	0	0

\* It should be noted that the possible Landlord Stock Voluntary Transfer has been ignored in the above calculation but this will be taken into account once the result of the ballot is known.

**PART 1**

**SECTION B – MATTERS FOR INFORMATION**

**ITEM 3**

**INSURANCE RENEWALS 2009/10**

The Authority's Insurance Policies are due for renewal on the 1<sup>st</sup> October 2009.

The Authority's Insurance Advisors are currently in the process of receiving and collating the individual insurance company proposals. However this information will only be finalised on 25<sup>th</sup> August 2009 and a further report will be tabled at the meeting showing the renewals quotations for the period 1<sup>st</sup> October 2009 to 30<sup>th</sup> September 2010.

**Officer Contact**

Mr. Hywel Jenkins – Head of Financial Services  
Tel. No. 01639 763646  
E-mail: [h.jenkins@npt.gov.uk](mailto:h.jenkins@npt.gov.uk)

**List of Background Papers**

Insurance Renewal Report 2009/10 by Marsh Insurance Consultants

**Wards Affected**

All.

**PART 1**  
**SECTION B – MATTERS FOR INFORMATION**

**ITEM 4**

**TREASURY MANAGEMENT**

**1. Purpose of Report.**

This report sets out treasury management action and information since the previous report.

**2. Long Term Borrowing.**

There has been no long term borrowing since the previous report.

**3. Rates of Interest.**

3.1. The Bank Rate:

<b>Effective Date</b>	<b>Bank Rate</b>
10 April 2008	5.00%
08 October 2008	4.50%
06 November 2008	3.50%
04 December 2008	2.00%
08 January 2009	1.50%
05 February 2009	1.00%
<b>05 March 2009 to date</b>	<b>0.50%</b>

3.2 Public Works Loans Board.

Examples of Public Works Loan Board new loan fixed interest rates effective on 11<sup>th</sup> August 2009:



	Equal Instalments of Principal		Annuity		Maturity	
	Current 11 Aug 09	Previous 02 Jul 09	Current 11 Aug 09	Previous 02 Jul 09	Current 11 Aug 09	Previous 02 Jul 09
		%		%		%
<i>5 to 5.5 years</i>	2.31	2.39	2.34	2.41	3.24	3.22
10 to 10.5 years	3.24	3.22	3.31	3.28	4.01	3.92
15 to 15.5 years	3.72	3.63	3.82	3.72	4.29	4.34
20 to 20.5 years	4.01	3.92	4.11	4.06	4.39	4.53
25 to 25.5 years	4.18	4.16	4.28	4.32	4.42	4.60
35 to 35.5 years	4.36	4.46	4.41	4.57	4.46	4.65
49.5 to 50 years	4.42	4.60	4.44	4.63	4.40	4.63

#### 4. Icelandic Bank Creditor Claims

Members will recall the collapse of the Icelandic banking system in October 2008, freezing £20m of Neath Port Talbot CBC investments.

Efforts to recover all funds have continued since the collapse with the Local Government Association co-ordinating negotiations on behalf of affected UK Local Authorities. The Icelandic Government has stated its intention to honour all its commitments as a result of their banks being placed into receivership, and indications are that most of the outstanding amounts will be recovered.

##### UK Subsidiaries

Creditor claims for principal plus interest have been submitted by the Authority to the Administrators of the Icelandic Banks UK subsidiaries, Kaupthing Singer and Friedlander and Heritable Bank.

In July 2009 the first distributions were paid to creditors and payments totalling £2.1m were received by this Authority as follows:

24 Jul 09	Kaupthing Singer and Freidlander	£0.6m
30 Jul 09	Heritable Bank	<u>£1.5m</u>
	<b>TOTAL</b>	<b><u>£2.1m</u></b>

## Icelandic Banks

Claims for principal and interest in respect of Glitnir and Landsbanki Islands HF are being completed by Bevan Britan Solicitors who are acting on behalf of UK authorities affected by the Icelandic banking collapse. Creditor claims are to be registered with the Icelandic Authorities before 26<sup>th</sup> November 2009 and 30<sup>th</sup> October 2009 respectively.

### **List of Background Papers**

PWLB notice 170/09

Treasury Management

### **Wards Affected**

All

### **Officer Contact**

For further information on this report item, please contact:

Mr. Hywel Jenkins - Head of Financial Services

Tel. No. 01639 763646

E-mail: [h.jenkins@npt.gov.uk](mailto:h.jenkins@npt.gov.uk)

Mr. Mark Davies - Chief Accountant (Corporate, Capital & Risk  
Management)

Tel. No. 01639 763602

E-mail: [m.davies4@npt.gov.uk](mailto:m.davies4@npt.gov.uk)