

**GREATER MANCHESTER INTEGRATED TRANSPORT AUTHORITY**

**REPORT FOR RESOLUTION**

**REPORT TO** Authority  
**DATE** 19 June 2009  
**SUBJECT** Treasury Management Annual Report 2008-09  
**REPORT OF** Finance Officer

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**PURPOSE OF REPORT**

To report the Treasury Management activities of the ITA during 2008-09.

**RECOMMENDATIONS**

The ITA is asked to note the report.

**FINANCIAL CONSEQUENCES FOR THE REVENUE BUDGET**

None.

**FINANCIAL CONSEQUENCES FOR THE CAPITAL BUDGET**

None.

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**Background Documents**

Treasury Management Strategy Statement and Borrowing Limits for 2008-09 and Prudential Indicators 2008-09 to 2010-11 (Authority 20 March 2008)

Treasury Management Revised Prudential Indicators 2008-09 (Authority 17 October 2008)

Accounting and Financial records are held in room 115.

## 1 Introduction and Background

1.1 Treasury Management in Local Government is regulated by the CIPFA Code of Practice on Treasury Management in Local Authorities. The ITA has adopted the Code and complies with its requirements. A primary requirement of the Code is the formulation and agreement by the Authority itself of a Treasury Policy Statement which sets out ITA and Finance Officer responsibilities, together with delegation and reporting arrangements. This was updated and approved by the Authority on 5 December 2003.

1.2 A requirement of the Treasury Policy Statement is the reporting to the ITA of both the expected treasury activity for the forthcoming financial year (the Treasury Management Strategy Statement 2008-09 and Borrowing Limits and Prudential Indicators 2008-09 to 2010-11) and, subsequently, the results of the Authority's treasury management activities in that year (this report). Treasury Management in this context is defined as:

"The management of the local authority's cash flows, its borrowings and its investments, the management of the associated risks, and the pursuit of the optimum performance or return consistent with those risks".

1.3 This annual report covers:

- the current portfolio position as at 31<sup>st</sup> March 2009
- the outturn for 2008-09
- treasury borrowing in 2008-09
- compliance with treasury limits and Prudential Indicators
- investment strategy for 2008-09
- investment outturn for 2008-09

## 2 Current Portfolio Position as at 31 March 2009

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

Loan Type	31 March 2008		31 March 2009	
	Principal £m	Average Rate %	Principal £m	Average Rate %
PWLB	80.1	8.90	182.6	6.41
Temporary	0	0	0	0
Market Loans	119.9	4.30	119.9	4.30
<b>Gross Total</b>	<b>200.0</b>	<b>6.14</b>	<b>302.5</b>	<b>5.57</b>
Temporary Deposits - Market	(46.5)	5.56	(112.0)	2.91
Temporary Deposits – M.C.C			(20.00)	0.50
Temporary Deposits - Interbank	(20.5)	5.88	(21.00)	0.98
<b>Net Total</b>	<b>133.0</b>	<b>6.38</b>	<b>149.5</b>	<b>8.89</b>

It should be noted that the accounting practice required to be followed by the Authority (the SoRP), changed in 2007/8 accounts, and required financial instruments in the accounts (debt and investments etc.) to be measured in a method compliant with national Financial Reporting Standards. The figures in this report are based on the amounts borrowed and invested and so may differ from those in the final accounts by items such as accrued interest.

### **3 Outturn for 2008-09**

- 3.1 On 1st April 2008, 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 CPI (Consumer Prices Index), 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 the spread between Bank Rate and 3 month LIBOR was greater than had historically been the case.

This phase continued throughout the summer, until the 15th September, when 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. 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. 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, RBS, HBOS and Lloyds, as liquidity in the markets dried up. The Monetary Policy Committee, meantime, had reduced interest rates by 0.50% 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.

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 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 at the longer end because of the economic consequences of reducing inflation, driving yields in 10 year PWLB temporarily below 4% and 5 years to around 3.5%. In December, 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.

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.

In 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. In early March, 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 that 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 have allowed indebted local authorities to benefit.

3.2 The movement in short and long-term interest rates for the year is shown in Appendix 1 Average PWLB interest rates for 2008/09 were as follows :

1 month variable	3.682%
1 year	3.264%
9.5 – 10 year	4.477%
25 – 30 year	4.570%
49.5 – 50 year	4.438%

#### 4 Treasury Borrowing in 2008-09

4.1 In total, £102.5m was borrowed from the PWLB in 2008-09, as follows :

Date	Principal	Rate	Period of loan
15 Aug 08	£20,000,000	4.58%	30 years
15 Aug 08	£20,000,000	4.39%	50 years
29 Aug 08	£5,000,000	4.60%	29.5 years
29 Aug 08	£10,000,000	4.59%	29 years
29 Aug 08	£5,000,000	4.59%	30.5 years
09 Oct 08	£5,000,000	4.59%	18.5 years
09 Oct 08	£5,000,000	4.57%	20.5 years
09 Oct 08	£5,000,000	4.54%	22 years
09 Oct 08	£5,000,000	4.52%	24 years
09 Oct 08	£5,000,000	4.45%	27 years
09 Oct 08	£2,500,000	4.36%	50 years
08 Dec 08	£5,000,000	4.15%	14.5 years
08 Dec 08	£5,000,000	4.23%	16.5 years
08 Dec 08	£5,000,000	4.05%	30 years
<b>Total</b>	<b>£102,500,000</b>	<b>4.46%</b>	

4.3 All new borrowings in 2008-09 have been taken out at below the target Metrolink 3a interest rate of 4.8%. These borrowings were taken out over the summer to fund the projected non grant funded Metrolink 3a expenditure.

4.4 No other new long-term borrowing was undertaken during 2008-09 because it became apparent that the Metrolink 3a cash flows were being revised and there was no requirement for further borrowings.

4.5 The table in paragraph 2.1 above shows that the end of year average rate of interest payable has decreased, from 6.14% as at 31 March 2008 down to 5.57% as at 31 March 2009. This was mainly due to the PWLB new borrowing above being undertaken at lower rates of interest than PWLB loans previously borrowed. The full year average rate of interest payable has reduced from 6.16% in 2007-08 down to 5.82% in 2008-09.

#### 4 Compliance with Treasury Limits

4.6 During the financial year, the ITA operated within the treasury limits and Prudential Indicators set out in its Treasury Policy Statement and annual Treasury Strategy Statement, as approved by the Authority on 20 March 2008. Revised Prudential Indicators were submitted to and approved by the ITA on 17 October 2008. The outturn for the Prudential Indicators is shown in Appendix 2.

## 5 Investment Strategy for 2008-09

4.7 The ITA's temporary cash balances are managed by the Finance Officer in-house and invested with those institutions listed in its Approved Lending List. The Authority invests for a range of periods from overnight to 364 days, dependent on its cash flow estimates and the interest rates on offer. All funds are invested with mainstream UK institutions with further use of the Debt Management Office.

4.8 The GMPTE Finance Department manages the Interbank Deposits on behalf of the GMITA. The Interbank Deposits included some Irish banks which have now been repaid in full.

## 6 Investment Outturn for 2008-09

4.9 Detailed below is the result of the investment strategy undertaken by the Authority and the Executive, (for Interbank.)

	Average Investment	Net Return	Benchmark Return *
Temporary Investments incl. Manchester City Council and Interbank	£118.9m	5.13%	3.69%

The table in paragraph 2.1 shows that the end of year average rate of interest receivable has reduced from 5.66% as at 31 March 2008 down to 2.20% as at 31 March 2009. The full year average rate of interest receivable has reduced from 5.96% in 2007-08 down to 5.13% in 2008-09.

\* Average 7-day LIBID rate (uncompounded) sourced from the Financial Times.

4.10 The GMITA had no investments with Icelandic banks at the time they went into receivership, nor did any other institutions in which investments were made show any difficulty in repaying investments and interest in full during the year. During the year investments of £1.5m and £3.5m with Icelandic banks both matured on 30 June 2008. The list of institutions in which the Authority invests is kept under continuous review.

## 8 Conclusion

8.1 Proactive treasury management during the year has enabled us to achieve an average net return on our investments of 5.13%, which is significantly better than the Benchmark Average 7-day LIBID rate of 3.69%. The end of year average interest receivable on our investments is 2.20%.

In addition, the average rate of interest payable on the Authority's overall debt during the year was 5.82%. The end of year average interest payable on our debt is 5.57%.

The net result of the interest earned on deposits and interest payable on borrowings has been a £3.2m. improvement against budget.