

Cumbria Police Authority

28 June 2005

Agenda Item No. 26

Treasury Management Activities for the period February 2006 to May 2006

Treasury Management Annual Report for 2005-06.

A report by the Treasurer and Chief Constable

1. Summary

- 1.1 The purpose of this paper is to report on the Treasury Management activities which have taken place between February and May 2006 and also to provide a brief annual report on the treasury function for the 2005-06 financial year. Both elements of the report are requirements of the Code of Practice on Treasury Management.

2. Recommendations

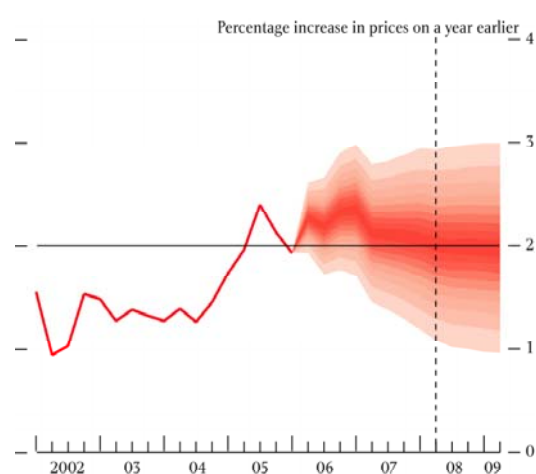
- 2.1 Members are asked to note the contents of the report.

3. Economic Background

- 3.1 The bank of England Monetary Policy Committee (MPC) again elected not to change the base interest rates at their meeting of June 7 and 8. Base rates have now remained at 4.5% since August 2005, subsequent to sitting at 4.75% for the previous twelve months. The latest available minutes of monthly MPC meetings, for the session held in May provide evidence of the rationale behind that decision. In summary, the arguments for the immediate future of interest rates appear to have been finely balanced. On the one hand, the arguments in favour of higher rates referenced the recent increases in output from a range of business surveys impacting on the rate of growth, the recent significant increases in energy prices and higher import prices as posing a risk of higher inflation, if current rates were not increased.
- 3.2 But on the other hand, some MPC members argued that consumption was below recent assumptions and that growth would increase below assumed rates, leaving a degree of spare capacity in the economy, which would require rates to be reduced to stimulate future growth. Whilst members attached different weightings to the arguments, most felt that the arguments were finely balanced, both in terms of projections for growth and also for inflation. Accordingly, the Committee agreed to leave interest rates unchanged, and have since done this again in June.

- 3.2 So far as the immediate future for interest rates is concerned, the current favoured view from analysts reflects the recent MPC debate as outlined above. The most recent quarterly inflation report, published in May, and debated by MPC, pointed to the recent impact of recent higher energy and import costs as increasing inflation above the 2% target, as reflected in the latest CPI measurement in May of 2.2%, although as these indices fall back in the longer term as expected, it is felt that the inflation target will move back to around its 2% target figure. Current CPI inflation projections, based on market rate expectations, are shown graphically below for members' information.

CPI Inflation projections based on market interest rate expectations



Source: Bank of England Inflation Report, May 2006.

With the general feeling, as set out in the inflation report, that interest rates are likely to meet their longer term target of 2%, the current belief amongst analysts is for interest rates to remain relatively static around their current rate of 4.5%. This is consistent with the forecast as set out in the Treasury Management strategy as approved by members in February. The chart at **Appendix one** outlines recent actual and future forecast rates.

4. Treasury Management operations and Performance Measures

4.1 Management of cash balances

Members are reminded that the aim is to invest surplus cash and minimise the level of uninvested cash balances whilst following the Treasury Management Strategy to limit risks to the Authority's funds. Actual uninvested balances for the months of February, March, April and May 2006 are shown graphically at **Appendix two** and summarised in the table below: -

	Number	Average Balance (£)	Largest Balance (£)
Days in Credit	107	17,665	1,401,421
Days Overdrawn	13	5,295	49,233

The largest surplus was on 28 February when a number of District Council precepts arrived in the Authority's bank account too late to be included in the daily cash investment process. Interest foregone amounted to £173. To avoid similar future occurrences, the finance team are looking to secure improvements to the investment software, which would alert relevant staff to late lodgements of income.

In addition, on 28 March, the large uninvested sum referred to in the appendix came about when a significant amount of cash was received too late in the day to place in the money market.

4.2 Interest Earned

Interest earned for the period of the report is set out in the table below: -

Month	Amount (£)
February 2006	81,531
March 2006	91,633
April 2006	89,512
May 2006	100,866

Total income in 2005-06 amounted to £1,050k, and is dealt with at paragraph six below.

The investment income budget for the 2006-07 financial year amounts to £810k. It is rather too early in the financial year to predict with certainty the actual level of investment income that will actually be achieved. Some of the key factors that will influence the total include movements in bank base rates during the year, which are forecast elsewhere in the report, investment income from the Authority's changing general and earmarked reserves and, critically, the scale and timing of payments for capital schemes.

4.3 Investment Performance

- 4.3.1 The table below shows the investment performance for investments of three months and beyond during the period of the report, based on a comparison with a benchmark rate, using LIBID [London Inter Bank Bid (Rate)].

Borrower	Value £(m)	Period (Months)	Actual Rate (%)	LIBID (%)
Norwich and Peterborough	2	6	4.55	4.50
Dexia	0.5	6	4.54	4.50
Alliance and Leicester	2	6	4.51	4.48
Derbyshire BS	2	12	4.6	4.57
West Bromwich BS	1	3	4.52	4.46
Coventry BS	2	6	4.56	4.53
Principality BS	1	6	4.58	4.54
Chelsea BS	1	12	4.67	4.65
West Bromwich BS	1	3	4.55	4.52
Bank of Ireland	2	6	4.65	4.62
Nationwide BS	2	12	4.87	4.82

Members should note that, on each occasion of the period covered by the report, the benchmark rate of interest has been exceeded.

6 Annual Report on Treasury Management Operations 2005-06

6.1 Strategy

6.1.1 At the start of the 2005-06 financial year, base rates stood at 4.75%, and remained relatively static throughout the year, moving only once, to 4.5% in August 2005. This was in slight contrast to the predictions for interest rates as set out in the 2005-06 Annual investment strategy, which suggested that rates might increase to about 5% perhaps by the end of the calendar year, before moving back, perhaps early in 2006-07. Based on the original forecast, investment returns were estimated at £690k.

6.1.2 Reflecting additional factors outlined at paragraph 6.3, actual income for the year amounted to £1,050k. This was in keeping with the projections given to members during the year and particularly during the latter months as set out below: -

Police Authority meeting	Amount (£'000)
September 2005	860
December 2005	1,000
February 2006	1,000+

6.2 Management of Treasury Risk

A fundamental part of the Authority's approach to managing treasury risk, as endorsed in the Treasury Management Strategy, is to ensure the safety of the public funds which are invested on behalf of the Authority. In 2005-06, as in previous years, this risk has been managed by: -

- (i) Keeping the credit ratings of the institutions we could potentially do business with under regular review. To this end changes are made to the schedule of investing counterparties twice yearly
- (ii) Reviewing the limits on the value of investments to individual institutions
- (iii) Reviewing the limits on sectors of the money market to avoid the possibility of any overdependence on any one type of financial institution.

Changes made as a result of the most recent review have been reflected in the 2006-07 annual Treasury Management Strategy.

6.3 Key Statistics 2005-06

- (i) Income from investments

	Amount (£'000)
Original Budget	690
Final Outturn	1,050

The additional income is a reflection of a number of factors as set out below: -

- (a) Commitments to a number of capital schemes has been deferred in light of the proposals for police amalgamations until such time as the future is more certain
- (b) More cash was available for investment due to a combination of slippage in the capital programme and planned contributions to a number of earmarked reserves
- (c) The need to forecast and budget prudently for a budget area where a number of uncertainties exist, in order to minimise the risk to the Authority's finances.

- (ii) Investments made

The cumulative value of investments made during the year amounted to £302m (or nearly £1m per day).

(iii) Balances after investment

Balances after investment for the 2005-06 financial year are set out in the table below.

	Number	Average Balance (£)	Largest Balance (£)
Days in credit	343	16,427	1,575,661
Days overdrawn	22	4,761	49,233

Explanations relating to the days with the largest uninvested balance and daily overdraft were provided during the year as part of the relevant quarterly activity report. However, to remind members: -

- (i) the largest uninvested balance occurred when one of the Authority's monthly payments of National Insurance contributions was not released on the due date, although the transaction was allowed for cash management purposes. No loss was suffered as HM Revenue and Customs did not claim any interest foregone.
- (ii) the largest overdrawn balance occurred when the Authority's bankers transferred an incorrect sum to one of our investment accounts. The Authority has been properly compensated for this oversight.

These statistics help to demonstrate overall performance of the Treasury Management function.

Douglas Thomas
Treasurer

Michael Baxter
Chief Constable

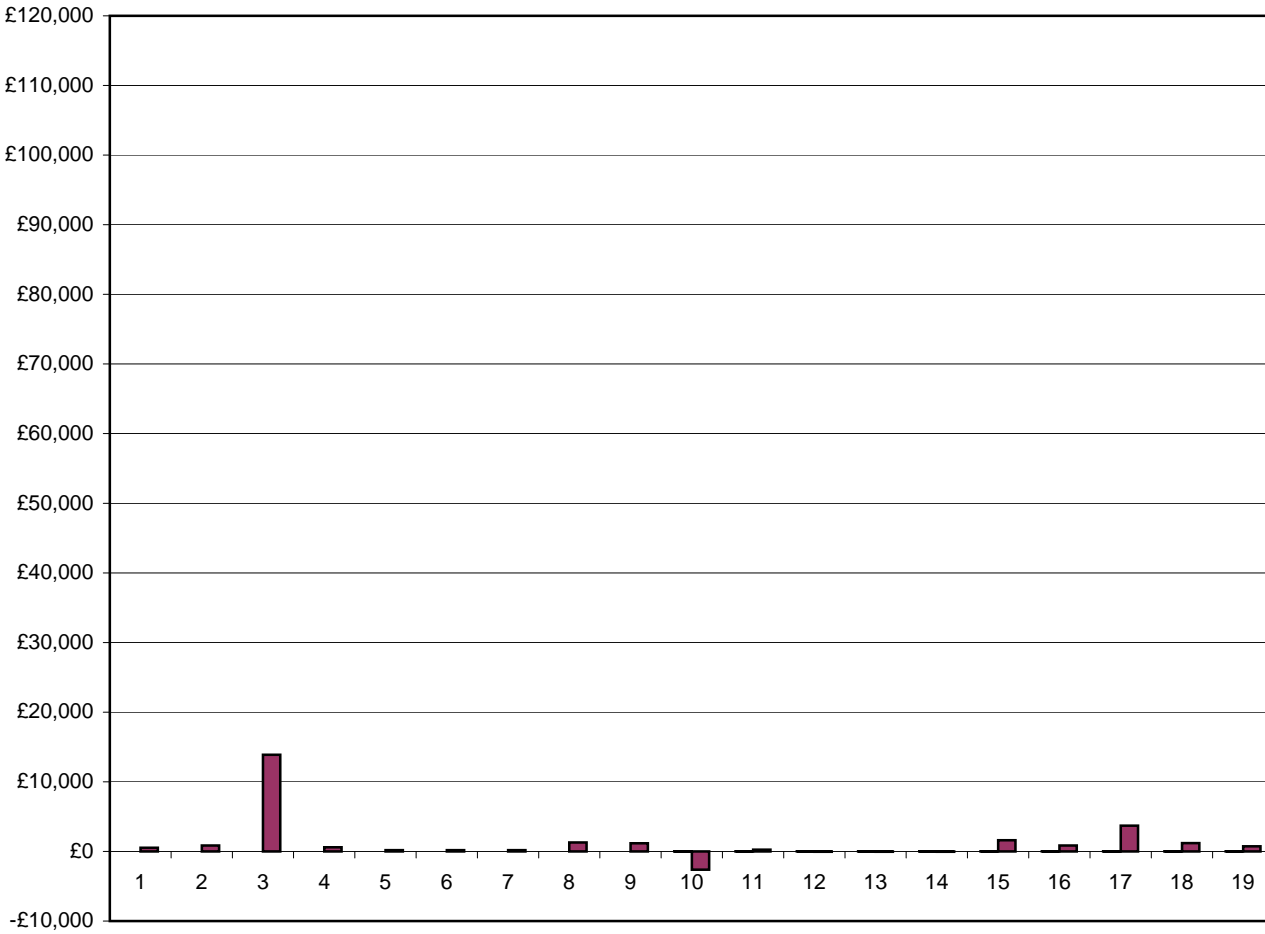
Contact point for information

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Attachments

- Appendix 1 Recent history and projections of Bank Base Rates
- Appendix 2 Monthly investment charts for February, March, April and May

**Cumbria Police Authority
May 2006 Clearing Balances**



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