SOUTH CAMBRIDGESHIRE DISTRICT COUNCIL

REPORT TO:	Finance and Staffing Portfolio Holder	17 February 2010
AUTHOR/S:	Executive Director (Corporate Services)/ Head of Accountancy	

INVESTMENT STRATEGY (TREASURY MANAGEMENT) 2010/11

Purpose

1. To recommend to Council the Investment Strategy for 2010/11.

2. This is a key decision because:
- it is likely to result in the Council incurring expenditure which is, or the making of savings which are, significant having regard to the Council's budget for the service or function to which the decision relates.
- it is of such significance to a locality, the Council or the services which it provides that the decision-taker is of the opinion that it should be treated as a key decision.

and it was first published in the February 2010 Forward Plan.

Background

3. With effect from 1st April 2004, the Local Government Act 2003:

(i) included a power for a local authority to invest for the purposes of prudent management of its financial affairs;

(ii) requires a local authority to have regard to any guidance the Secretary of State may issue; and

(iii) repealed all the previous legislation on approved investments.

Considerations

4. Draft revisions to investment guidance were issued in November 2009 by Department for Communities and Local Government (DCLG). The main changes in the draft revised guidance are:

(i) the guidance makes even clearer that the investment priorities should be **security** and **liquidity**, rather than yield;

(ii) investment strategies should still go to the full council at the start of each year, but authorities are encourages to consider submitting revised strategies at other times;

(iii) strategies should be published;

(iv) authorities should not rely just on credit ratings but consider also other information on credit risk;

(v) strategies should comment on the use of treasury management consultants; and

(vi) strategies should comment on the investment of money borrowed in advance of spending needs.

5. The Chartered Institute of Public Finance and Accountancy (CIPFA) has also issued in November 2009 a fully revised second edition of its Treasury Management in the Public Services Code of Practice which identifies three key principles:

   1) public service organisations should put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury management activities;

   2) their policies and practices should make clear that the effective management and control of risk are prime objectives of their treasury management activities and that responsibility for these lies clearly within their organisations. Their appetite for risk should form part of their annual strategy and should ensure that priority is given to security and liquidity when investing funds; and

   3) they should acknowledge that the pursuit of value for money in treasury management, and the use of suitable performance measures, are valid and important tools for responsible organisations to employ in support of their business and service objectives; and that within the context of effective risk management, their treasury management policies and practice should reflect this.

6. The proposed investment strategy for 2010/11 is attached as **Appendix A**. The proposed strategy does **not** comply with the Code which, as a minimum, stipulates for reports annually to full Council on the investment strategy <u>and</u> plan, a mid year position report and an end of year performance report.

7. The investment strategy sets out the limits within which Council officers must operate. Once the strategy is approved, the Head of Accountancy issues a list of approved organisations/counterparties within each category in the investment strategy, with which the Council can invest. This list is reviewed during the year to take account of:

   (a) mergers of organisations which are reducing the number of counterparties with which the Council can invest;

   (b) the current economic climate whereby organisations which are allowed in accordance with the investment strategy are suspended from the list of approved organisations, e.g. in the category of other banks and financial institutions, the three Irish banks and the Icelandic bank, Landsbanki Islands, are currently suspended; and

   (c) the credit rating and financial standing of approved organisations which, where available, are checked before any investment decision is made.

8. The Prudential Code for Capital Finance in Local Authorities requires local authorities to set prudential indicators before the beginning of the financial year. These indicators include liquidity of investments, interest rate exposure, etc., were reported to Cabinet on 11th February 2010 and are repeated as an appendix to the investment strategy.

Options

9. These include:

(a) Continuing with the present policy which has produced good results. The Council is a member of the CIPFA Treasury Management benchmarking club. The results for 2008/09 show that South Cambridgeshire achieved a return of 5.61% on combined investments (less than and more than 365 days) compared to 5.36% for its comparator group and 5.26% for the overall group. South Cambridgeshire was third highest in the comparator group of 13 other organisations and nineteenth highest in the overall group of 128 other organisations. These good results were achieved at minimal cost;

(b) Adopting a risk free strategy by investing only with the Debt Management Office which is a government agency and should be totally secure. Interest rates with this organisation are generally substantially lower than rates in the money market and this would result in substantially lower interest on balances than the figure which is in the 2010/11 estimates;

(c) Increasing risk which should produce a higher rate of return. This is not recommended;

(d) With the rapidly declining level of capital receipts, outsourcing is probably no longer feasible as external fund managers often require at least £10 million for at least three years; and

(e) An option would be to stop using lists of named counterparties and have a policy of investing only with counterparties with an AAA or similar rating (except for public sector bodies). This would be a radical departure from present practice and would probably result in investing with foreign banks and other commercial organisations (but with all investments and repayments still denominated in £ sterling). Most of these organisations will only accept a minimum of £5 million so the Council would, therefore, have fewer higher value investments with the consequent higher risk arising from less diversification. With reducing balances, the opportunity for these large investments will be very limited.
A policy of investing only with counterparties with an AAA rating would be heavily dependent on the credit rating being an accurate assessment. Standard & Poor's Guide to Credit Rating Essentials states that "credit ratings are not investment advice" and "credit ratings are not guarantees of credit quality or of future credit risk".
In addition to using the credit rating of organisations, some councils are also taking in to account the sovereign rating of the country where the organisation is based in another country.

Implications

10.

Financial	The Council may currently earn less interest on its investments by having a very restricted range of investments but this is considered to be more than offset by the reduced risk of default by counterparties.
Legal	None
Staffing	The use of credit ratings requires some research by staff who deal with treasury management.

Risk Management	There is internal check with division of duties between dealing, administration and authorisation and any losses due to fraud should be covered by fidelity guarantee insurance. Credit and counterparty risk is currently managed by restricting the range of investment organisations to the main banks, building societies, etc. The use of credit ratings places greater reliance on the credit rating agency/ies which do not provide any indemnities against loss.
Equal Opportunities	None

Effect on Strategic Aims

11.

Commitment to being a listening council, providing first class services accessible to all.	To determine the budget and council tax to provide the resources for the Council to continue its services to achieve its strategic aims as far as possible within the current financial constraints.
Commitment to ensuring that South Cambridgeshire continues to be a safe and healthy place for all.	
Commitment to making South Cambridgeshire a place in which residents can feel proud to live.	
Commitment to assisting provision for local jobs for all.	
Commitment to providing a voice for rural life.	

Recommendations

12. The Portfolio Holder is requested to recommend to Council the Investment Strategy for 2010/11 in the Appendix and to request that the Portfolio Holder be given delegated authority to make minor amendments to the Strategy in the event that the final guidance from the DCLG differs from the draft guidance.

Background Papers: the following background papers were used in the preparation of this report:

Draft revisions to investment guidance from the DCLG dated 16th November 2009
Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (CIPFA) fully revised second edition 2009

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