


**AGENDA ITEM NO:**

**UNIVERSITY HOSPITALS BIRMINGHAM NHS FOUNDATION TRUST  
REPORT TO THE BOARD OF DIRECTORS  
THURSDAY 23 FEBRUARY 2012**

<b>Title:</b>	<b>CHANGES TO THE TREASURY MANAGEMENT POLICY</b>
<b>Responsible Director:</b>	Mike Sexton, Director of Finance
<b>Contact:</b>	Julian Miller, Deputy Director of Finance, ext. 53074

<b>Purpose:</b>	To present an update to the Board
<b>Confidentiality Level &amp; Reason:</b>	N/A
<b>Medium Term Plan Ref:</b>	Aim 2: Maintain our reputation and position at the leading edge of performance and quality Aim 3: Enhance our reputation for excellent financial management and efficiency
<b>Key Issues Summary:</b>	For the last 12 months the Trust has held its entire cash balance in its Barclays current account. It is now possible to achieve better rates of return by placing some cash in fixed term investments however this will require changes to the current Treasury Management Policy.
<b>Recommendations:</b>	The Board of Directors is asked to: <ul style="list-style-type: none"><li>• Approve the proposed changes to the Treasury Management Policy</li></ul>

<b>Signed:</b> 	<b>Date:</b> 10 February 2012
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# UNIVERSITY HOSPITALS BIRMINGHAM NHS FOUNDATION TRUST

## REPORT TO THE BOARD OF DIRECTORS THURSDAY 23 FEBRUARY 2012

### CHANGES TO THE TREASURY MANAGEMENT POLICY

#### PRESENTED BY THE DIRECTOR OF FINANCE

#### 1. Introduction

The investment of surplus cash by the Trust is governed by the Treasury Management Policy. This policy is based on Monitor's guidance 'Managing Operating Cash within NHS Foundation Trusts', which provides advice on the investment of surplus operating cash that may be needed within 12 months to support ongoing operations. Longer term cash investments are subject to separate mandatory guidance.

Over the last 12 months all of the Trust's cash has been held in the Barclays current account which has offered competitive rates of interest. This rate is reducing slightly in 2012 and it is now possible to get significantly better returns by investing cash in fixed term deposits for either 3, 6, 9 or 12 months. However, in order to realise these benefits it will be necessary to make some changes to the Treasury Management Policy as detailed below. The proposed changes were discussed and supported by the Investment Committee on 20 December 2011.

#### 2. Treasury Management Policy

##### 2.1 Current Policy

The Trust's current Treasury Management Policy was only approved in December 2010 but this has already been superseded by market events including the recent downgrading of the credit ratings held by all UK high street banks.

The key features of the current policy are:

- The types of investment are cash based only e.g. money market deposits, certificates of deposit and instant access investment accounts.
- These investments must be in GBP sterling only.
- The Trust cannot enter into any investment business, hold shares, foreign exchange or commodities for the purpose of trading, nor enter into any contract or option for such business.
- The maximum term for investments is limited to 3 months duration.
- The Trust is only permitted to invest in banks with a Moody's long term rating of Aaa or Aa1 (or equivalent) and up to defined maximum amounts - £15m GBP for a UK bank and £10m for a

foreign bank. These limits were set prior to the banking crisis of 2008.

Following the latest market downgrading of many banks in October 2011, all UK high street banks are now excluded by the current policy. For example, using the Moody's ratings, HSBC are Aa2 (1 level below Aa1) and Barclays are Aa3 (2 levels below) Lloyds are A1 (3 levels below) and RBS are A2 (4 levels below).

It should be noted that the Treasury Management Policy applies to term deposits only and does not restrict the balances held in the Trust's main current accounts with Barclays and Government Banking Services (GBS) as these are instant access.

## 2.2 Proposed Changes

In order to provide the Trust with the flexibility to utilise investment products to achieve a greater return than is offered by its current account it is proposed that a number of changes are made to the Treasury Management Policy:

- The minimum bank rating is decreased from Aa1 to A1. This covers all Aa rated institutions (Aa1 to Aa3) and the best A rated institutions (A1). Although this represents a decrease of 3 levels, Moodys describe the entire Aa rating category as 'obligations judged to be of high quality and subject to very low credit risk'. The numerical modifier only determines the relative ranking of an investment within the overall category class. Similarly all A rated obligations are defined as 'upper medium grade and are subject to low credit risk'. This would meet Monitor's definition of safe harbour products which states that long term ratings should be A1 or above. This change is necessary for practical purposes with the entire sector having been downgraded.
- Investments are restricted to major high street banks incorporated in the UK (UK clearing banks) only. This provides a further safeguard as precedent suggests that these institutions are likely to be supported by the UK government in the event of the risk of default.
- The maximum value held by any single applicable bank is increased from £15m to £25m.
- The maximum term is extended from 3 months to 12 months to obtain the best available rates. The Monitor guidance does not stipulate a maximum term for cash investments, although the definition of 'Safe Harbour investments' only extends to products with maturity dates of up to 3 months. However Monitor have recently confirmed that any investments deemed to be current assets (realisable within one year) by the Trust's external auditors can be included for the purposes of calculating the liquidity ratio (part of the Trust's Financial Risk Rating).

It is intended that the Treasury Management Policy will be subject to a full review in June 2012, as originally scheduled, which will incorporate the changes outlined above should they be approved.

### **3. Financial Analysis**

#### **3.1 Current Performance**

Total interest income of £702,455 was recorded in 2010/11 and £557,000 has been recognised in the first 9 months of 2011/12.

During 2011 Barclays have paid 1.5% on the first £10m held in the current account and 0.9% on balances above this amount. This will reduce slightly in 2012 with only 0.8% paid on balances above £10m. The Trust had a cash balance of £64.2m at 31 December 2011 and the minimum daily bank balance over the past 12 months has not fallen below £57.1m.

#### **3.2 Alternative Options**

Instead of leaving surplus cash in the Barclays Bank current account, the option is available to the Trust to place a sum of money on deposit for up to 12 months, through either a 'certificate of deposit' or 'fixed term money deposit'. Current rates of interest are circa 1.85% for one year. This represents an increase of 105 basis points over the 0.8% paid by the Barclays current account.

On this basis, each £10m invested for 12 months would earn £185,000 as opposed to £80,000 remaining in the current account. As an example: £25m GBP would earn interest income of £462,500 over 1 year at 1.85% as opposed to £200,000 if earning 0.8% in the Barclays current account.

### **4. Other Investment Considerations**

#### **4.1 Operating Cash Requirements**

One of the main aims of the Treasury Management Policy is to ensure that the Trust has sufficient liquidity to meet operating cash flow requirements at all times without recourse to external funding such as the working capital facility. Therefore any investment decisions must be planned carefully with due consideration for future cash requirements.

#### **4.2 PDC Dividend Calculation**

The investment of surplus cash is usually constrained by the calculation of PDC dividends payable to the Department of Health by NHS organisations. Trusts are required to transfer their cash to the Government Banking Service (GBS) on 31 March, in order for this asset to be excluded from the 3.5% PDC dividend charge for the cost of capital. This normally precludes investments which span the year-end. However the current balance sheet of the Trust has negative

liabilities (due to the accounting impairment of the new PFI hospital) and therefore at present all the Trust's surplus cash could in theory be held by a commercial banking institution on 31 March 2012 without requiring a PDC dividend to be paid.

## 5. **Proposed Investment Approach**

It is proposed that the Trust builds a portfolio of products to achieve the best available rates (12 month deposits) whilst maintaining flexibility in terms of liquidity. This could be achieved by taking out four initial deposits for 3, 6, 9 and 12 months respectively. In 3 months time when the first deposit matures this would be replaced by a new 12 month deposit and so forth. After the first year the entire balance would be achieving 12 month interest rates but a quarter of the total would always be available within a maximum of 3 months. This would ensure sufficient flexibility to respond to cash requirements or market trends and review future investments accordingly.

In line with the Treasury Management Policy, the amounts to be invested would be recommended by the Financial Controller and the Deputy Director of Finance and approved by the Director of Finance.

## 6. **Conclusion**

For the last 12 months the Trust has held its entire cash balance in its Barclays current account. It is now possible to achieve better rates of return on by holding part of this balance on fixed term deposits, however this will require a number of changes to the current Treasury Management Policy as outlined above. The proposed changes were discussed and supported by the Investment Committee on 20 December 2011.

## 7. **Recommendations**

The Board of Directors is asked to:

- Approve the proposed changes to the Treasury Management Policy



Mike Sexton  
Director of Finance  
10 February 2012