

# Report

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Report to:	<b>Finance and Information Technology Resources Committee</b>
Date of Meeting:	<b>14 June 2011</b>
Report by:	<b>Chief Executive</b>

Subject:	<b>Treasury Management – Use of Money Market Funds</b>
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## 1. Purpose of Report

1.1. The purpose of the report is to:-

- ◆ Provide an explanation of Money Market Funds and how they can be used as a means of managing cash flow.

## 2. Recommendation(s)

2.1. The Committee is asked to approve the following recommendation(s):-

- (1) that approval is given for Treasury Management to use Money Market Funds as a means of managing the cash flow requirements of South Lanarkshire Council.

## 3. Background

4.1. South Lanarkshire Council's Annual Investment Strategy for 2011/12 was approved by full Council on 10 February 2011. Money Market Funds are included in the Annual Investment Strategy as a permitted investment but, to date, have not been used.

## 4. Use of Money Market Funds

4.1. Money Market Funds (MMFs) are pooled funds that invest in the short term money market in instruments such as deposits, Government Bonds and commercial paper (which are effectively deposits with banks and corporations). These funds allow investors to participate in a more diverse and high-quality portfolio than if they were to invest individually.

4.2. Each investor in a money market fund is considered a shareholder of the investment pool, or a part owner of the fund. All investors in a money market fund have a claim on a pro-rata share of the fund's assets in line with the number of 'shares' or 'units' owned.

4.3. It should be noted that the assets of MMFs belong to the shareholders, not the company that administers the Fund. The assets are separate and ring fenced and would not be considered in the event that a MMF administrator company wound up.

4.4. In addition to these limits, all MMFs employ their own credit analysts who will carry out their own independent assessment of whether an investment is suitable and appropriate

## **5. Use of Money Market Funds by South Lanarkshire Council**

- 5.1. South Lanarkshire Council's Annual Investment Strategy for 2011/12, approved by full Council on 10 February 2011, includes MMFs as a permitted investment.
- 5.2. In managing the Council's cash flow position, surplus cash is currently deposited in banks and building societies that meet the Council's counterparty requirements as detailed in the Annual Investment Strategy. The Council also used the Government's Debt Management Office (DMO) deposit account and we have approval to purchase Treasury Bills from the government. MMFs can offer higher interest rates than some banks and the DMO without increasing the risk to the Council.
- 5.3. It is recommended that approval is given for Treasury Management to begin to use MMFs as a means of managing the cash flow requirements of South Lanarkshire Council.
- 5.4. Investments will be restricted to MMFs that have obtained a AAA rating for MMFs from the credit rating agencies and a maximum of £10m will be placed with any one MMF. This is in accordance with the criteria set out in the Annual Investment Strategy.
- 5.5. Advice will be taken from the Council's Treasury Management Advisers when selecting particular MMFs in which to deposit funds.
- 5.6. A Money Market Fund, known as the Public Sector Deposit Fund has been established specifically for local authorities and other public sector organisations and was launched in May 2011.
- 5.7. This Money Market Fund will be considered along with other MMFs, but will only be used once its suitability can be assessed and if it meets the criteria set out in the Annual Investment Strategy.

## **6. Risk**

- 6.1. As with any Treasury Management activity, it is recognised that risk cannot be removed completely, but steps can be taken to reduce or mitigate the risk.
- 6.2. **Counterparty Risk** – The use of money market funds mitigates counterparty risk by means of diversification. A deposit placed with a MMF is spread across a number of high quality investments. If one counterparty was to default, only a small proportion of the deposit would be lost.
- 6.3. Counterparty risk will be further mitigated by only using MMFs that have obtained a AAA rating from the credit rating agencies and by placing a maximum of £10m with any one MMF.
- 6.4. In addition to the credit rating, funds will also be assessed for suitability on fund size and the strength of the custodian.
- 6.5. **Liquidity Risk** – MMFs mitigate liquidity risk by providing same day liquidity, ensuring that the Council has access to funds when required.

- 6.6. **Market Risk** – changes to interest rates can cause the value of the underlying investments in a MMF to fluctuate. There are different types of MMF, however we will only use MMFs which work to maintain each £1 of investment at £1 in order to protect our initial investment. Interest will be paid on top on the investment depending on the performance of the Fund
- 7. Employee Implications**
- 7.1. There are no employee implications.
- 8. Financial Implications**
- 8.1. Any return made from depositing or investing surplus funds offsets Loan Charges made to the Council's Revenue budget.
- 9. Other Implications**
- 9.1. Section 6 of this report provides details of the risks inherent in any Treasury Management activity of the Council and how these are mitigated or controlled through the use of MMFs.
- 10. Equality Impact Assessment and Consultation Arrangements**
- 10.1. This report does not introduce a new policy, function or strategy or recommend a change to an existing policy, function or strategy and, therefore, no impact assessment is required.
- 10.2. There is also no requirement to undertake consultation in terms of the information contained in this report.

**Archibald Strang**  
**Chief Executive**

17 May 2011

**Link(s) to Council Values/Improvement Themes/Objectives**

- ◆ Accountable, effective and efficient

**Previous References**

- ◆ Finance and Information Technology Resources Committee 1 February 2011

**List of Background Papers**

- ◆ Annual Investment Strategy 2011/12

**Contact for Further Information**

If you would like to inspect the background papers or want further information, please contact:-

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