



CABINET

8 February 2012

Subject Heading:

Cabinet Member:

CMT Lead:

Report Author and contact details:

Policy context:

Financial summary:

Is this a Key Decision?

Is this a Strategic Decision?

When should this matter be reviewed?

Reviewing OSC:

REPORT

Treasury Management Strategy Statement, Minimum Revenue Provision Policy Statement and Annual Investment Strategy 2012/13

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The Council is required to formally approve the Treasury Management Strategy Statement, Minimum Revenue Provision Policy Statement and the Annual Investment Strategy following recommendation from Cabinet

There are no direct financial implications from the strategy. Treasury management activities are considered as part of the overall budget strategy.

No

No

Bi-Annually

Audit Committee

The subject matter of this report deals with the following Council Objectives

Ensuring a clean, safe and green borough	<input type="checkbox"/>
Championing education and learning for all	<input type="checkbox"/>
Providing economic, social and cultural activity	<input type="checkbox"/>
in thriving towns and villages	<input type="checkbox"/>
Valuing and enhancing the lives of our residents	<input type="checkbox"/>
Delivering high customer satisfaction and a stable council tax	<input checked="" type="checkbox"/>

SUMMARY

The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals. These reports are required to be adequately scrutinised by committee before being recommended to the Council. This role is undertaken by the Audit Committee.

Prudential and Treasury Indicators and Treasury Strategy (This report) - The first, and most important report covers:

- the capital plans (including prudential indicators);
- a Minimum Revenue Provision Policy (how residual capital expenditure is charged to revenue over time);
- the Treasury Management Strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

A Mid Year Treasury Management Report – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether the treasury strategy is meeting the strategy or whether any policies require revision.

An Annual Treasury Report – This provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

RECOMMENDATIONS

Cabinet to agree the Treasury Management Strategy Statement (TMSS) which incorporates the MRP Strategy and the Annual Investment Strategy 2012/13 and to recommend to full Council that the TMSS be approved.

REPORT DETAIL

Please refer to Appendix A for the Treasury Management Strategy Statement which incorporates the Minimum Revenue Provision Policy Statement and the Annual Investment Strategy.

REASONS AND OPTIONS

Reasons for the decision:

The statutory Codes set out that the Council ought to approve a Treasury Management Strategy Statement, the MRP Strategy and the Annual Investment Strategy for 2012/13.

Other options considered:

There are no good reasons to depart from the provisions of the relevant Codes.

IMPLICATIONS AND RISKS

Financial implications and risks:

There are no direct financial implications arising from this report. Treasury management activities are considered as part of the overall budget strategy

Legal implications and risks:

There are no apparent legal implications arising as a result of this Report.

Human Resources implications and risks:

There are no direct Human Resources implications arising as a result of this report

Equalities implications and risks:

There are no equalities implications within this report

BACKGROUND PAPERS

- 1 CIPFA Prudential Code
 - 2 CIPFA Treasury Management Code of Practice
 - 3 Sector Treasury Services Economic Outlook
 - 4 Bloomberg System
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Appendix A – Treasury Management Strategy Statement

1 Introduction

1.1 Background

The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

CIPFA defines treasury management as:

“The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.”

1.2 Treasury Management Strategy

The strategy for 2012/13 covers two main areas:

Capital Issues

- the capital plans and the prudential indicators;
- the MRP strategy.

Treasury management Issues

- the current treasury position;
 - treasury indicators which will limit the treasury risk and activities of the Council;
 - prospects for interest rates;
 - the borrowing strategy;
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- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the CLG MRP Guidance, the CIPFA Treasury Management Code and the CLG Investment Guidance.

2. The Capital Prudential Indicators 2012/13 – 2014/15

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans are reflected in prudential indicators, which are designed to assist members overview and confirm capital expenditure plans.

A key issue facing the Council is the impact of planned HRA reform. This would essentially end the impact of the housing subsidy system and will see the HRA as a stand alone business. The legislation has yet to be enacted, but the Council will need to approve revised limits in expectation of the reform going ahead.

The Council currently pays into the HRA housing subsidy system, and in order to stop future payments from 1 April 2012 the Council is required to pay the CLG £166m. This payment is effectively HRA debt, and so the prudential indicators have been adjusted to reflect this change. The actual payment will be made on the 28 March 2012 and so the indicators will take immediate effect from the approval of these limits by Council. The change is expected to be beneficial to the Council.

Capital Expenditure. This prudential Indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding need (borrowing).

Capital Expenditure £m	2010/11 Actual	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
Non-HRA	60.964	58.378	29.329	10.110	8.188
HRA	16.433	20.011	24.000	24.000	32.500
HRA settlement		166.206*			
Total	77.397	244.595	53.329	34.110	40.688
Financed by:					
Capital receipts	9.178	27.448	16.278	6.123	4.201
Capital grants	42.414	29.647	28.051	18.987	27.487
Capital reserves	6.276	8.780	0	0	0
Revenue	3.115	2.048	0	0	0
Net financing need for the year	16.414	176.672	9.000	9.000	9.000

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*HRA Settlement figure as per paragraph above

The Council's Borrowing Need (the Capital Financing Requirement)

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

Following accounting changes the CFR includes any other long term liabilities (e.g. PFI schemes, finance leases) brought onto the balance sheet. Whilst this increases the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes.

£m	2010/11 Actual	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
Capital Financing Requirement					
CFR – non housing	50.259	48.931	47.603	46.275	50.517
CFR - housing	13.050	23.517	32.517	41.517	44.947
HRA Settlement		166.206	166.206	166.206	166.206
Total CFR	63.309	238.654	246.326	253.998	261.670
Movement in CFR	15.192	175.345	7.672	7.672	7.672

Movement in CFR represented by					
Net financing need for the year (above)	16.414	176.672	9.000	9.000	9.000
HRA Settlement					
Less MRP/VRP and other financing movements	1.222	1.327	1.328	1.328	1.328
Movement in CFR	15.192	175.345	7.672	7.672	7.672

MRP Policy Statement

The Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP), although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

CLG Regulations have been issued which require the full Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement:

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For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be:

- **Existing practice** - MRP will follow the existing practice outlined in former CLG regulations (option 1)

This option provides for an approximate 4% reduction in the borrowing need (CFR) each year.

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

- **Asset Life Method** – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3);

These options provide for a reduction in the borrowing need over approximately the asset's life.

No revenue charge is currently required for the HRA. However under HRA reform the HRA will be required to charge depreciation on its assets, which will have a revenue effect. In order to address any possible adverse impact, regulations will allow the Major Repairs Allowance to be used as a proxy for depreciation for the first five years.

Affordability Prudential Indicators

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances:

Actual and estimates of the ratio of financing costs to net revenue stream.

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

%	2010/11 Actual	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
Non-HRA	1.52	1.47	1.19	1.11	0.87
HRA (inclusive of settlement)	4.31	6.47	5.27	5.27	5.27

The estimates of financing costs include current commitments and the proposals in this budget report.

Estimates of the incremental impact of capital investment decisions on council tax.

This indicator identifies the revenue costs associated with proposed changes to the three year capital programme recommended in this budget report compared to the Council's existing approved commitments and current plans. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which are not published over a three year period.

£	2010/11 Actual	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
Council tax - band D	4.26	4.26	0.00	0.00	0.00

Estimates of the incremental impact of capital investment decisions on housing rent levels.

Similar to the council tax calculation, this indicator identifies the trend in the cost of proposed changes in the housing capital programme recommended in this budget report compared to the Council's existing commitments and current plans, expressed as a discrete impact on weekly rent levels.

£	2010/11 Actual	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
Weekly housing rent levels	0.00	0.00	0.00	0.00	0.00

This indicator shows the revenue impact on any newly proposed changes, although any discrete impact will be constrained by rent controls.

3. Treasury Management Strategy

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The treasury management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

3.1 Current Portfolio Position

The Council's treasury portfolio position at 31 March 2011, with forward projections are summarised below. The table shows the actual external borrowing (the treasury management operations), against the capital

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borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

£m	2010/11 Actual	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
External borrowing					
Borrowing at 1 April	46.08	59.86	212.15	221.15	230.15
Expected change in borrowing	13.78	(13.91)	9.00	9.00	9.00
HRA settlement	0	166.20	0	0	0
Other long-term liabilities (OLTL)	0	0	0	0	0
Expected change in OLTL	0	0	0	0	0
Actual borrowing at 31 March	59.86	212.15	221.15	230.15	239.15
CFR – the borrowing need	63.31	238.65	246.32	254.00	261.67
Under / (over) borrowing	3.45	26.50	25.17	23.85	22.52
Investments	91.47	47.42	44.52	44.52	44.52
Net borrowing	(28.16)	191.23	176.63	185.63	194.63

Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well defined limits. One of these is that the Council needs to ensure that its total borrowing, net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2012/13 and the following two financial years (shown as net borrowing above). This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Director of Finance reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

3.2. Treasury Indicators: Limits to Borrowing Activity

The Operational Boundary. This is the limit beyond which external borrowing is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual borrowing.

Operational boundary £'000	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
Borrowing	75,000	89,800	98,800	106,800
Add HRA settlement	200,000	166,200	166,200	166,200
Other long term liabilities	2,000	2,000	2,000	2,000
Total	277,000	258,000	267,000	275,000

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*the 2011/12 prudential indicators were based on estimates as final HRA settlement figures had not been published

The Authorised Limit for external borrowing. A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external borrowing is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

1. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

Authorised limit £'000	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
Borrowing	95,000	102,800	111,800	120,800
Add HRA settlement	200,000	166,200	166,200	166,200
Other long term liabilities	2,000	2,000	2,000	2,000
Total	297,000	271,000	280,000	289,000

*the 2011/12 prudential indicators were based on estimates as final HRA settlement figures had not been published

3.3. Prospects for Interest Rates

The Council has appointed Sector as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. The following table gives the Sector central view.

Annual Average %	Bank Rate	Money Rates		PWLB Borrowing Rates		
		3 month	1 year	5 year	25 year	50 year
March 2012	0.50	0.70	1.50	2.30	4.20	4.30
June 2012	0.50	0.70	1.50	2.30	4.20	4.30
Sept 2012	0.50	0.70	1.50	2.30	4.30	4.40
Dec 2012	0.50	0.70	1.60	2.40	4.30	4.40
March 2013	0.50	0.75	1.70	2.50	4.40	4.50
June 2013	0.50	0.80	1.80	2.60	4.50	4.60
Sept 2013	0.75	0.90	1.90	2.70	4.60	4.70
Dec 2013	1.00	1.20	2.20	2.80	4.70	4.80
March 2014	1.25	1.40	2.40	2.90	4.80	4.90
June 2014	1.50	1.60	2.60	3.10	4.90	5.00

Growth in the UK economy is expected to be weak in the next two years and there is a risk of a technical recession (i.e. two quarters of negative growth). Bank Rate, currently 0.5%, underpins investment returns and is not expected to start increasing until quarter 3 of 2013 despite inflation currently being well above the Monetary Policy Committee inflation target. Hopes for an export

led recovery appear likely to be disappointed due to the Eurozone sovereign debt crisis depressing growth in the UK's biggest export market. The Comprehensive Spending Review, which seeks to reduce the UK's annual fiscal deficit, will also depress growth during the next few years.

Fixed interest borrowing rates are based on UK gilt yields. The outlook for borrowing rates is currently much more difficult to predict. The UK total national debt is forecast to continue rising until 2015/16; the consequent increase in gilt issuance is therefore expected to be reflected in an increase in gilt yields over this period. However, gilt yields are currently at historically low levels due to investor concerns over Eurozone sovereign debt and have been subject to exceptionally high levels of volatility as events in the Eurozone debt crisis have evolved.

This challenging and uncertain economic outlook has a several key treasury management implications:

- The Eurozone sovereign debt difficulties, most evident in Greece, provide a clear indication of much higher counterparty risk. This continues to suggest the use of higher quality counterparties for shorter time periods;
- Investment returns are likely to remain relatively low during 2012/13;
- Borrowing interest rates are currently attractive, but may remain low for some time. The timing of any borrowing will need to be monitored carefully;
- There will remain a cost of capital – any borrowing undertaken that results in an increase in investments will incur a revenue loss between borrowing costs and investment returns.

3.4 Borrowing Strategy

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is high and will be maintained for the borrowing excluding the HRA reform settlement.

Against this background and the risks within the economic forecast, caution will be adopted with the 2012/13 treasury operations. The Director of Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates, e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.*
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- *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.*

The requirement for the HRA reform settlement to be made to the CLG on 28 March 2012 will require a separate consideration of a borrowing strategy. The Council will need to have the cash settlement amount of £166.2m available by the 28th March 2012, so separate borrowing solely for this purpose is anticipated. The PWLB are providing loans at interest rates 0.85% lower than the usual PWLB interest rates solely for the settlement requirements. This provides a compelling reason to utilise this borrowing availability. The exact structure of debt to be drawn is currently being considered by officers to ensure it meets the requirements of the HRA business plan and the overall requirements of the Council. Whilst the debt can be drawn earlier than needed, this may incur a revenue cost, and will be considered when a review of the structure of actual prevailing borrowing and investment interest rates is undertaken nearer to the time.

Any decisions will be reported to the appropriate decision making body at the next available opportunity.

Treasury Management Limits on Activity

There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments
 - Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates;
 - Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.
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	2012/13	2013/14	2014/15
Interest rate Exposures			
	Upper	Upper	Upper
Limits on fixed interest rates based on net debt	100%	100%	100%
Limits on variable interest rates based on net debt	25%	25%	25%
Maturity Structure of long term borrowing 2012/13			
	Lower	Upper	
Under 12 months	0%	40%	
12 months to 2 years	0%	40%	
2 years to 5 years	0%	60%	
5 years to 10 years	0%	75%	
10 years and above	0%	100%	

3.5 Policy on Borrowing in Advance of Need

The Council will not borrow more, than or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Borrowing in advance will be made within the constraints that:

- It will be limited to no more than 50% of the expected increase in borrowing need (CFR) over the three year planning period; and
- Would not look to borrow more than 12 months in advance of need.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

3.6. Debt Rescheduling

As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings;
 - helping to fulfil the treasury strategy;
 - enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).
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Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be reported to the Audit Committee, at the earliest meeting following its action.

3.7. Annual Investment Strategy

Investment Policy

The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, then return.

In accordance with the above, and in order to minimise the risk to investments, the Council has below clearly stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list. The creditworthiness methodology used to create the counterparty list fully accounts for the ratings and watches published by all three ratings agencies with a full understanding of what the ratings reflect in the eyes of each agency. Using the Sector ratings service banks' ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications.

Further, the Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "Credit Default Swaps" and overlay that information on top of the credit ratings. This is encapsulated within the credit methodology provided by the advisors, Sector.

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk.

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The intention of the strategy is to provide security of investment and minimisation of risk.

Investment instruments identified for use in the financial year are listed below in the 'Specified' and 'Non-Specified' Investments categories. Counterparty limits will be as set through the Council's Treasury Management Practices – Schedules.

Creditworthiness policy

The Council applies a 2 stage approach when establishing its creditworthiness policy.

Stage 1

The Council uses a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the duration for investments. The Council will therefore use counterparties within the following durational bands:

- Yellow 5 years *
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 3 months
- No Colour not to be used

** this category is for AAA rated Government debt or its equivalent*

Typically the minimum credit ratings criteria the Council use will be a short term rating (Fitch or equivalents) of Short Term rating F1, Long Term rating A-, Individual of Viability ratings of C- (or BB+), and a Support rating of 3. There may be occasions when the counterparty ratings from one rating

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agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored on a daily basis and prior to any significant deposits. The Council is alerted to changes to ratings of all three agencies through its use of the Sector creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Stage 2

The list of eligible counterparties from stage 1 will then be reviewed by the Lead Member and the Group Director for Finance & Commerce on a quarterly basis where a shortened, revised list of eligible counterparties will be established and an appropriate duration limit placed on each.

Any changes to the final list of eligible counterparties will need approval from both the lead Member and the group director for Finance & Commerce

By using this 2 stage process, sole reliance will not be placed on the use of the Authorities treasury advisers. In addition the Council will also be using the latest market data and market information, information on government support for banks and the credit ratings of that government support when assessing which banks will be eligible for deposits under the second stage.

In addition to the above criteria, it is proposed that the counterparty listing will include :

- UK guaranteed institutions. The maximum duration of deposit will depend on the guarantee from the UK government in place.
 - The Council's banker for deposits via the current and liquidity account. No new fixed term deposits would be made, should the ratings not meet the above criteria.
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Country limits

The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA+ from Fitch. Due care will be taken when considering the country exposure of the Council's investments. No more than £10m will be placed with any non UK country at any one time.

Group & Institution Limits

The Council has the following group & institution limits in place:

- UK institutions – group limit the lower of £25m or 25% of the investments opening balance at the start of the quarter
- Any foreign institution - maximum of £5m
- Local Authorities – maximum of £50m with no more than £10m with any one Authority
- Debt Management Office – maximum of £100m
- Triple A rated Government Bond Funds and/or AAA rated Money market Funds (MR1+), maximum of £25m.

Investment Instruments

Investment Instruments can be split into 2 categories, specified investments and non-specified investments:

Specified Investments - These investments are sterling investments of not more than one-year maturity, or those which could be for a longer period but where the Council has the right to be repaid within 12 months if it wishes. These are considered low risk assets where the possibility of loss of principal or investment income is small.

Non-Specified Investments – Non-specified investments are any other type of investment (i.e. not defined as Specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below.

A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories. Listed below are the types of specified and non-specified investments allowable under this treasury strategy:

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Specified Investments	* Minimum credit criteria / colour band	£ limit per institution	Max. maturity period
DMADF – UK Government	N/A	£100m	6 months
Money market funds / Government Liquidity Funds	Long-term AAA volatility rating MR1+	£25m	Liquid
Local authorities	N/A	£10m	Up to 1 year
Term deposits with banks and building societies	Blue Orange Red Green No Colour	See group and institution limits above	Up to 1 year Up to 6 Months Up to 3 months Not for use
CDs or corporate bonds with banks and building societies	Blue Orange Red Green No Colour	See group and institution limits above	Up to 1 year Up to 6 Months Up to 3 months Not for use

Non-Specified Investments	* Minimum credit criteria / colour band	£ limit per institution	Max. maturity period
Term deposits with banks and building societies	Yellow Purple	See group and institution limits above	Up to 5 years Up to 2 years
CDs or corporate bonds with banks and building societies	Yellow Purple	See group and institution limits above	Up to 5 years Up to 2 years
Local authorities	N/A	£10m	5 years
Bonds issued by multilateral development banks	AAA	£10m	Up to 6 months
Collateralised deposit (see note 1)	UK sovereign rating	£10m	5 years
UK Government gilts	AAA	£10m	5 years
UK Government Treasury bills	AAA	£10m	5 years

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Note 1. as collateralised deposits are backed by collateral of AAA rated local authority LOBOs, this investment instrument is regarded as being a AAA rated investment as it is equivalent to lending to a local authority.

Investment Returns

Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 3 of 2013. Bank Rate forecasts for financial year ends (March) are:

- 2011/ 2012 0.50%
- 2012/ 2013 0.50%
- 2013/ 2014 1.25%
- 2014/ 2015 2.50%

There are downside risks to these forecasts (i.e. start of increases in Bank Rate is delayed even further) if economic growth remains weaker for longer than expected. However, should the pace of growth pick up more sharply than expected there could be upside risk, particularly if Bank of England inflation forecasts for two years ahead exceed the Bank of England's 2% target rate.

The suggested budgeted investment earnings rates for returns on investments placed for periods up to three months during each financial year for the next five years are as follows:

2012/13	1.00%
2013/14	1.00%
2014/15	1.60%
2015/16	3.30%
2016/17	4.10%

Investment treasury indicator and limit - total principal funds invested for greater than 364 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

Maximum principal sums invested > 364 days			
£m	2012/13	2013/14	2014/15
Principal sums invested > 364 days	£75	£75	£75

Icelandic Bank Investments – The Icelandic courts have supported the view that the Council will be treated as a preferred creditor, thereby seeing a high proportion of the investment being returned. The actual repayment is currently expected to be partially in foreign currency assets. It is currently too early to provide a definitive policy on how this exchange rate risk will be managed, but the expectation will be that the risk will be managed proactively and assets converted to sterling at the earliest opportunity.

3.8 End of year investment report

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

3.9 Policy on the use of external service providers

The Council uses Sector as its external treasury management advisors.

The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

3.10 Scheme of delegation

(i) Full Council

- receiving and reviewing reports on treasury management policies, practices and activities;
- approval of annual strategy.

(ii) Audit Committee

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
 - budget consideration and approval;
 - approval of the division of responsibilities;
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- receiving and reviewing regular monitoring reports and acting on recommendations;
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Lead Member

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

3.11 Role of the section 151 officer

The S151 (responsible) officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
 - submitting regular treasury management policy reports;
 - submitting budgets and budget variations;
 - receiving and reviewing management information reports;
 - reviewing the performance of the treasury management function;
 - ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
 - ensuring the adequacy of internal audit, and liaising with external audit;
 - recommending the appointment of external service providers.
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