COUNCIL - APPENDIX 4

NORTH WEST LEICESTERSHIRE DISTRICT COUNCIL

CABINET – 11 FEBRUARY 2014

Title of report	**THE TREASURY MANAGEMENT STRATEGY STATEMENT 2014/15 AND PRUDENTIAL INDICATORS 2014/15 TO 2016/17**
Key Decision	a) Financial Yes b) Community Yes
Contacts	Councillor Nick Rushton 01530 412059 nicholas.rushton@nwleicestershire.gov.uk Chief Executive 01530 454500 christine.fisher@nwleicestershire.gov.uk Head of Finance 01530 454520 ray.bowmer@nwleicestershire.gov.uk
Purpose of report	This report outlines the expected treasury operations for the forthcoming financial year and sets out the Authority's prudential indicators for 2014/15 to 2016/17. It fulfils the key requirements of the Local Government Act 2003: • The Treasury Management Strategy Statement in accordance with the CIPFA Code of Practice for Treasury Management in Public Services ; • The Annual Investment Strategy in accordance with the CLG Investment Guidance; • The reporting of the prudential indicators as required by the CIPFA Prudential Code for Capital Finance in Local Authorities. • The Policy for the Annual Minimum Revenue Provision.
Reason for Decision	These are statutory requirements.
Council Priorities	Value for Money
Implications: Financial/Staff Link to relevant CAT Risk Management	 Interest earned on balances and interest paid on external debt, impacts on the resources available to the Authority. Could impact upon all CAT's. Borrowing and investment both carry an element of risk. This risk is moderated through the adoption of the Treasury and Investment Strategies, compliance with the CIPFA Code of Treasury Management and the retention of Treasury Management Advisors (Arlingclose) to proffer expert advice.
Equalities Impact Assessment	Not applicable.

Human Rights	Not applicable.
Transformational Government	Not applicable.
Comments of Head of Paid Service	The report is satisfactory
Comments of Section 151 Officer	The report is satisfactory
Comments of Monitoring Officer	The report is satisfactory
Consultees	None.
Background papers	The "Annual Treasury Management Stewardship Report 2008/09 and Re-Adoption of the CIPFA Revised Code of Practice and Treasury Management Policy Statement" – Cabinet 16 June 2009 The "Housing Revenue Account (HRA) Business Plan" – Cabinet 13 March 2012 http://prod-modgov:9070/mgCommitteeDetails.aspx?ID=126
Recommendations	**IT IS RECOMMENDED THAT CABINET:** **1) RE-ADOPT THE CIPFA TREASURY MANAGEMENT IN PUBLIC SERVICES: CODE OF PRACTICE;** **AND** **2) RECOMMEND THE TREASURY MANAGEMENT STRATEGY STATEMENT 2014/15, PRUDENTIAL INDICATORS -REVISED 2013/14 AND 2014/15 TO 2016/17, AND THE ANNUAL MINIMUM REVENUE PROVISION STATEMENT, FOR APPROVAL BY FULL COUNCIL**

1.0 INTRODUCTION

1.1 The Chartered Institute of Public Finance and Accountancy's Treasury Management in Public Services Code of Practice (the "CIPFA TM Code") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators (PIs) on an annual basis. The TMSS also includes the Annual Investment Strategy (AIS) that is a requirement of the CLG's Investment Guidance.

1.2 As per the requirements of the Prudential Code, the Authority adopted the CIPFA Treasury Management Code of Practice at a meeting of the Cabinet on 16 June 2009. The revised CIPFA Treasury Management in The Public Services Code of Practice was published in 2011. The clauses that were adopted in 2009 remain the same under the revised code and are re-submitted for Council approval (Appendix A).

1.3 CIPFA has defined Treasury Management as: "the management of the organisation'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."

1.4 The TMSS and prudential indicators ensure that the Authority complies with statutory, regulatory, and professional (CIPFA) requirements.

The TMSS sets out:

a. Background information used to determine borrowing and investment requirements (paragraphs 2.2 and 2.3).
b. Organisational roles and responsibilities (paragraph 1.7).
c. The role of the Authority's treasury advisor (paragraph 1.8).
d. Reporting and monitoring of treasury management activity (paragraph 1.9).
e. Borrowing and debt rescheduling strategies. General Fund interest payments on existing debt are estimated at £505,694 in 2014/15.
f. Investment Strategy. Security of capital is the first and most important investment policy objective. Total investment income is estimated at £68,000 in 2014/15 (General Fund - £43k, HRA - £25k).
g. Treasury Management Prudential Indicators for 2014/15 to 2016/17. These are designed to monitor borrowing limits, debt levels and investment returns.

All treasury activity will comply with relevant statute, guidance and accounting standards.

1.5 The Authority is responsible for its treasury decisions and activity. No treasury management activity is without risk. The successful identification; monitoring and control of risk are important and integral elements of treasury management activities. The main risks to the Authority's treasury activities are:

- Credit and Counterparty Risk (security of investments)
- Liquidity Risk (inadequate cash resources)
- Market or Interest Rate Risk (fluctuations in interest rate levels)
- Inflation Risk (exposure to inflation)
- Refinancing Risk (impact of refinancing on suitable terms)
- Legal & Regulatory Risk (failure to act in accordance with powers or regulatory requirements)

1.6 The Treasury Management Strategy Statement reviews:

- the economic background and outlook for U.K. interest rates
- implications for treasury activity
- the Authority's current balance sheet and treasury position
- the Authority's Borrowing Strategy
- the Authority's Debt Restructuring Strategy
- the Authority's Investment Policy and Strategy
- the Authority's Interest Apportionment Policy
- the Authority's Prudential Indicators 2013/14 to 2016/17
- the Authority's Minimum Revenue Position.

1.7 Organisational Roles and Responsibilities

In accordance with CIPFA guidance, the roles and responsibilities of the Authority's Treasury Management function are divided between several responsible officers and are summarised below:

<u>Section 151 Officer</u> – overall responsibility for the treasury management function to include:

Ensuring the organisation of the treasury management function is adequate to meet current requirements:

- Investment, borrowing and debt rescheduling decisions.
- Monitoring adherence to approved Treasury Management Strategy Statement.
- Regular reporting to Members on Treasury Management activity.

Finance Team Manager (Deputy Section 151 Officer) – ensuring that day to day treasury activities comply with the approved Treasury Management Strategy Statement.

Technical Accountant – identification of investment opportunities and borrowing requirements and acts as the Authority's interface with brokers and counterparties.

1.8 The Role of the Authority's Treasury Advisor

The Authority currently employs Arlingclose Ltd. as treasury advisor to provide the following services; strategic treasury management advice, advice relating to Housing & Capital finance, economic advice and interest rate forecasting, debt restructuring and portfolio review (structure and volatility), counterparty credit ratings and other creditworthiness indicators and training, particularly investment training, for Members and officers.

Arlingclose Ltd is authorised and regulated by the Financial Conduct Authority (FCA). Arlingclose Ltd provide the Authority with timely, clear and regular information about the financial sector to enable the Authority to take pro-active decisions which in turn, helps to minimise risk.

1.9 Reporting and Monitoring of Treasury Management Activity

The Treasury Management Stewardship Report for 2013/14 will be presented to the Audit and Governance Committee for scrutiny and then Cabinet as soon as possible after the end of the financial year. As in previous years, the Treasury Management Strategy Statement will be supplemented by in-year reporting of treasury management activity and monitoring of prudential indicators, to the Audit and Governance Committee during 2014/15.

This report, together with all other reports to Council, Cabinet and the Audit and Governance Committee are a public record and can be viewed on the Authority's website. This demonstrates compliance with CLG Guidance on local government investments, which recommends that the initial strategy, and any revised strategy, should, when approved, be made available to the public free of charge, in print or online.

2.0 THE TREASURY MANAGEMENT STRATEGY STATEMENT 2014/15

2.1 The purpose of this Treasury Management Strategy Statement is to set out for approval

- The Borrowing Strategy 2014/15 (APPENDIX B)
- The Debt Rescheduling Strategy 2014/15 (APPENDIX C)
- The Annual Investment Strategy 2014/15 (APPENDIX D)
- The Apportionment of Interest Strategy 2014/15 (APPENDIX E)
- The Prudential Indicators 2014/15 to 2016/17 (APPENDIX F)
- The Annual Minimum Revenue Provision (APPENDIX G)

2.2 Economic Background.

- The Bank of England's Monetary Policy Committee (MPC) through its recent forward guidance is committed to keeping policy rates low for an extended period using the Labour Force Survey unemployment rate of 7% as a threshold for when it would consider whether or not to raise interest rates, subject to certain knock-outs. Unemployment was 7.4% in the three months to October 2013, but is not forecast to fall below the threshold until 2016, due to the UK's flexible workforce.
- The flow of credit to households and businesses is slowly improving but is still below pre-crisis levels. The fall in consumer price inflation from the high of 5.2% in September 2011 to 2.0% in December 2013 will allow real wage increases (i.e. after inflation) to slowly turn positive and aid consumer spending.
- Stronger growth data in 2013 (0.4% in Q1, 0.7% in Q2 and 0.8% in Q3) alongside a pick-up in property prices mainly stoked by government initiatives to boost mortgage lending have led markets to price in an earlier rise in rates than warranted under Forward Guidance and the broader economic backdrop. However, with jobs growth picking up slowly, many employees working shorter hours than they would like and benefit cuts set to gather pace, growth is likely to only be gradual. Arlingclose forecasts the MPC will maintain its resolve to keep interest rates low until the recovery is convincing and sustainable.
- In the US expectations for the slowing in the pace of asset purchases ('tapering') by the Federal Reserve and the end of further asset purchases will remain predominant drivers of the financial markets. The Federal Reserve did not taper in September and has talked down potential tapering in the near term. It now looks more likely to occur in early 2014 which will be supportive of bond and equity markets in the interim.
- Credit outlook: The credit risk of banking failures has diminished, but not dissipated altogether. Regulatory changes are afoot in the UK, US and Europe to move away from the bank bail-outs of previous years to bank resolution regimes in which shareholders, bond holders and unsecured creditors are 'bailed in' to participate in any recovery process. This is already manifest in relation to holders of subordinated debt issued by the Co-op which will suffer a haircut on its conversion bail-in to alternative securities and/or equity There are also proposals for EU regulatory reforms to Money Market Funds which will, in all probability, result in these funds moving to a VNAV (variable net asset value) basis and losing their 'triple-A' credit rating wrapper. Diversification of investments between creditworthy counterparties to mitigate bail-in risk will become even more important in the light of these developments.

2.3 Outlook for UK Interest Rates:

The Authority's treasury advisor's current central case forecast for the UK Bank Rate is set out below.

March 2014	**June 2014**	**Sept. 2014**	**Dec. 2014**	**March 2015**	**June 2015**	**Sept. 2015**	**Dec. 2015**	**March 2016**
0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%

The Authority's treasury advisor has forecast that the Bank Rate will remain flat until late 2016.

3.0 IMPLICATIONS FOR TREASURY ACTIVITY

3.1 The economic outlook, the financial health of sovereign states, major banks and investment counterparties and the regulatory changes that are anticipated, still provide major challenges and risk for treasury activity, particularly investment activity, during financial year 2014/15.

3.2 The principles in the proposed suite of treasury policies remain broadly unchanged from previous years - borrowing will be prudent, minimise borrowing costs and maintain the stability of the debt maturity portfolio. Debt rescheduling should achieve interest savings, carry minimal risk and maintain the stability of the debt maturity portfolio. Investments will be prioritised and based upon the principles of security, liquidity and yield.

3.3 The Treasury Management Strategy Statement will be monitored throughout the year and, if necessary, amended and brought back to Members for approval.

4.0 THE AUTHORITY'S CURRENT BALANCE SHEET AND TREASURY POSITION

4.1 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). Usable reserves and balances are the underlying resources available for investment. The CFR, balances and reserves are the core drivers of Treasury Management Activity. The estimates, based on the current Revenue Budget and Capital Programmes, are set out below:

	31 Mar 14 Estimate £m	**31 Mar 15 Estimate £m**	**31 Mar 16 Estimate £m**	**31 Mar 17 Estimate £m**
CFR	91.759	91.407	90.549	89.812
Balances & Reserves	6.000	6.000	6.000	6.000
Net Balance Sheet Position	85.759	85.407	84.549	83.812

4.2 The Authority's level of physical debt and investments is linked to these components of the Balance Sheet. Market conditions, interest rate expectations and credit risk considerations will influence the Authority's strategy in determining the borrowing and investment activity against the underlying Balance Sheet position. The Authority's current strategy is to maintain borrowing and investments below their underlying levels (internal borrowing).

4.3 CIPFA's 'Prudential Code for Capital Finance in Local Authorities' recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. The Authority expects to comply with this recommendation during 2014/15.

APPENDIX A

THE REVISED CIPFA CODE OF PRACTICE FOR TREASURY MANAGEMENT 2011

This Council re-adopts the four key recommendations of the CIPFA Code of Practice for Treasury Management.

1. The Council will create and maintain, as the cornerstones for effective treasury management:

    - A treasury management policy statement, stating the policies and objectives of its treasury management activities

    - Suitable treasury management practices (TMP's) setting out the manner in which the Council will seek to achieve those policies and objectives and prescribing how it will manage and control those activities.

2. The Council will receive reports on its treasury management policies, practices and activities including as a minimum, an annual strategy and plan in advance of the year, a midyear review and an annual report after its close, in the form prescribed in the TMP's.

3. The Council delegates responsibility for the implementation and monitoring of its treasury management policies and practices to the Cabinet and for execution and administration of treasury management decisions to the Section 151 Officer, who will act in accordance with the Council's policy statement and TMP's and CIPFA's Standard of Professional Practice on Treasury Management.

4. The Council's Audit and Governance Committee is responsible for ensuring effective scrutiny of the treasury management strategy, policies and activity.

APPENDIX B

BORROWING STRATEGY 2014/15

The Authority currently holds loans totalling £87.5m (£79.1m HRA and £9.4m General Fund). This is a decrease of £1m on the previous year (£80.1m HRA and £9.4m General Fund) and is part of the Authority's strategy for funding previous years' capital programme and for the self-financing of the HRA, which was presented to Cabinet on 17th January 2012 in the "Housing Revenue Account (HRA) Business Plan".

The Authority prefers to maintain maximum control and minimise risk over its borrowing activities whilst preserving flexibility on its loans portfolio. Capital expenditure levels, market conditions and interest rate levels will be monitored during the year in order to minimise borrowing costs over the medium to longer term. A prudent and pragmatic approach to borrowing will be maintained to minimise borrowing costs without compromising the longer-term stability of the portfolio, consistent with the Authority's Prudential Indicators.

Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, at this time it is more cost effective to borrow internally or on a short term basis.

By utilising internal or short-term borrowing, the Authority is able to reduce overall treasury risk and net borrowing costs, despite the foregone investment income. This is likely to be beneficial whilst official interest rates remain low however the benefits of this strategy will be monitored to ensure the most effective outcome for the Authority.

In addition, the Authority may borrow short-term loans to cover unexpected cash flow shortages.

The approved sources of long and short term borrowing are:

- Internal borrowing
- Public Works Loans Board
- UK local authorities
- Any institution approved for investments
- Any other bank or building society authorised by the Prudential Regulation Authority to operate in the UK.
- Capital market bond investors
- UK public and private sector pension funds (except Leicestershire County Council Pension Fund)
- Special purpose companies created to enable joint local authority bond issues

The Authority has previously raised the majority of its long-term borrowing from the Public Works Loan Board but it continues to investigate other sources of finance, such as local authority loans and bank loans that may be available at more favourable rates.

The Authority holds two LOBO (Lender's Option Borrower's Option) loans totalling £7.4m as part of its total borrowing of £87.5m, where the lender has the option to propose an increase in the interest rate at set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost. These LOBO's have options during 2014/15 and although the Authority understands that the lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk. The Authority will take the opportunity to repay LOBO loans at no cost if it has the opportunity to do so.

Borrowing activity will be reported in the annual Treasury Management Stewardship Report and supplemented with in-year Treasury Activity Reports to the Audit and Governance Committee.

APPENDIX C

DEBT RESCHEDULING STRATEGY 2014/15

The Authority will continue to maintain a flexible policy for debt rescheduling.

The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. However, the lower interest rate environment has adversely affected the scope to undertake meaningful debt restructuring although occasional opportunities arise. The rationale for rescheduling will be one or more of the following:

- Savings in interest costs with minimal risk.
- Balancing the volatility profile (i.e. the ratio of fixed to variable rate debt) of the debt portfolio.
- Amending the profile of maturing debt to reduce any inherent refinancing risks.

Any rescheduling activity will be undertaken within the Authority's Treasury Management Policy and Strategy. The Authority will agree in advance with its treasury advisor, the strategy and framework within which debt will be repaid / rescheduled, should opportunities arise. Thereafter, the Authority's debt portfolio will be monitored against equivalent interest rates and available refinancing options on a regular basis. As opportunities arise, they will be identified by the Authority's treasury advisor and discussed with the Authority's officers.

All rescheduling activity will comply with accounting and regulatory requirements and will be reported in the annual Treasury Management Stewardship Report and supplemented with in-year Treasury Activity Reports to the Audit and Governance Committee.

APPENDIX D

ANNUAL INVESTMENT STRATEGY 2014/15

Background

Guidance from CLG on Local Governments in England requires that an Annual Investment Strategy (AIS) be approved by Full Council.

Investment Policy

Both the CIPFA Code and the CLG Guidance require the Authority to invest its funds prudently. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. The Authority's investment priorities are:

- security of the invested capital;
- liquidity of the invested capital;
- An optimum yield which is commensurate with security and liquidity.

The Authority will not borrow money in advance of need for the purpose of investing at a higher rate. The speculative practice of borrowing purely in order to invest is unlawful.

Investment Strategy

There is no intention to restrict investments to bank deposits, and investments may be made with any public or private sector organisations that meet the Authority's counterparty criteria. This reflects a lower likelihood that the UK and other governments will support failing banks as the bail-in provisions in the *Banking Reform Act 2014* and the EU *Bank Recovery and Resolution Directive* are implemented. In addition, the Authority may invest with organisations and pooled funds without credit ratings, following an external credit assessment and advice from the Authority's treasury management adviser.

The Authority understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008 and 2011, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

The Authority compiles its cash flow forecast on a pessimistic basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Authority having to borrow on unfavourable terms. Limits on investments are set with reference to the Authority's Medium Term Financial Plan and cash flow forecast. This also determines the maximum period for which funds may prudently be committed.

The Section 151 Officer, under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators.

. **INVESTMENT GUIDANCE AND COUNTERPARTY CRITERIA**

In accordance with CLG Guidance, investments fall into two categories, Specified and Non-Specified.

<u>Specified Investments</u>: The CLG Guidance defines specified investments as those:

- Denominated in pound sterling
- has a maximum maturity of 1 year
- not defined as capital expenditure by Legislation
- invested with one of:
    - the UK Government
    - a UK local authority, parish council, community Council
    - a body or investment scheme of 'high credit quality'

The Authority defines 'high credit quality' organisations as those having a credit rating of A- or higher that are domiciled in the UK, or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds 'high credit quality' is defined as those having a credit rating of A- or higher.

<u>Non-Specified Investments</u>: Any investment not meeting the definition of a specified investment is classed as non-specified. The Authority does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition on high credit quality.

The Authority's investments are made with reference to the Authority's cash flow, the outlook for the UK Bank Rate, money market rates, the economic outlook and advice from the Authority's treasury adviser.

To minimise the risk of investment losses in the case of a default, the maximum that will be lent to any one organisation (other than the UK Government) will be £5 million. A group of banks under the same ownership or a group of funds under the same management will be treated as a single organisation for limit purposes. Limits will also be placed on investments in brokers' nominee accounts *(e.g. King & Shaxson)*, foreign countries and industry sectors as below:

	Cash limit
Any single organisation, except the UK Central Government	£5m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£5m per group
Any group of pooled funds under the same management	£5m per manager
Negotiable instruments held in a broker's nominee account	£5m per broker
Foreign countries	£5m per country
Registered Providers	£5m in total
Building Societies	£5m in total
Loans to small businesses	£2m in total
Money Market Funds	£15m in total

The Authority may lend or invest money using any of the following instruments:

- interest-bearing bank accounts
- fixed term deposits and loans
- callable deposits and loans where the Authority may demand repayment at any time (with or without notice)
- callable deposits and loans where the borrower may repay before maturity
- certificate of deposit
- bonds, notes, bills, commercial paper and other marketable instruments
- shares in money market funds and other pooled funds

Counterparty Criteria

The Authority may invest its surplus funds with any of the counterparties in the table below, subject to the limits shown:

<table>
<tr><th colspan="2">Counterparty</th><th>Cash limit</th><th>Time limit †</th></tr>
<tr><td rowspan="7">Banks, other organisations and securities whose lowest published long-term credit rating from Fitch, Moody's and Standard & Poor's is:</td><td>AAA</td><td rowspan="7">£5m each</td><td>10 years*</td></tr>
<tr><td>AA+</td><td>5 years*</td></tr>
<tr><td>AA</td><td>4 years*</td></tr>
<tr><td>AA-</td><td>3 years*</td></tr>
<tr><td>A+</td><td>2 years</td></tr>
<tr><td>A</td><td rowspan="2">1 year</td></tr>
<tr><td>A-</td></tr>
<tr><td colspan="2">UK Central Government (irrespective of credit rating)</td><td>unlimited</td><td>50 years**</td></tr>
<tr><td colspan="2">UK Local Authorities (irrespective of credit rating)</td><td>£5m each</td><td>50 years**</td></tr>
<tr><td colspan="2">UK Registered Providers of Social Housing whose lowest published long-term credit rating is A- or higher</td><td>£3m each</td><td>10 years**</td></tr>
<tr><td colspan="2">UK Registered Providers of Social Housing whose lowest published long-term credit rating is BBB- or higher and those without credit ratings</td><td>£2m each</td><td>5 years</td></tr>
<tr><td colspan="2">UK Building Societies without credit ratings</td><td>£1m each</td><td>1 year</td></tr>
<tr><td colspan="2">Money market funds and other pooled funds</td><td>£5m each</td><td>n/a</td></tr>
<tr><td colspan="2" rowspan="3">Any other organisation, subject to an external credit assessment and specific advice from the Authority's treasury management adviser</td><td>£3m each</td><td>3 months</td></tr>
<tr><td>£1m each</td><td>1 year</td></tr>
<tr><td>£100k each</td><td>5 years</td></tr>
</table>

† the time limit is doubled for investments that are secured on the borrower's assets

* but no longer than 2 years in fixed-term deposits and other illiquid instruments
** but no longer than 5 years in fixed-term deposits and other illiquid instruments

Current Account Bank: Following a competitive tender exercise held in 2013, the Authority's current account is held with Co-operative Bank Plc which is currently rated below the minimum A- rating. The Authority does not hold investments with this bank and manages the risk by maintaining an overnight balance that is estimated to be close to zero.

Registered Providers: Formerly known as Housing Associations, Registered Providers of Social Housing are tightly regulated by the Homes and Communities Agency and retain a high likelihood of receiving government support if needed. The Authority will consider investing with unrated Registered Providers with adequate credit safeguards, subject to receiving independent advice.

Building Societies: The Authority takes additional comfort from the building societies' regulatory framework and insolvency regime where, in the unlikely event of a building society liquidation, the Authority's deposits would be paid out in preference to retail depositors. The Authority will therefore consider investing with unrated building societies where independent credit analysis shows them to be suitably creditworthy. The Government has announced plans to amend the building society insolvency regime alongside its plans for wide ranging banking reform, and investments in lower rated and unrated building societies will therefore be kept under continuous review.

Money Market Funds: These funds are pooled investment vehicles consisting of money market deposits and similar instruments. They have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager. Fees of between 0.10% and 0.20% per annum are deducted from the interest paid to the Authority. Funds that offer same-day liquidity and aim for a constant net asset value will be used as an alternative to instant access bank accounts, while funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

Other Pooled Funds: If the Authority has substantial cash balances available for investment over the medium term, it will consider using pooled bond, equity and property funds that offer enhanced returns over the longer term, but are potentially more volatile in the shorter term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

Other Organisations: The Authority may also invest cash with other organisations, for example by making loans to small businesses. Because of the higher perceived risk of unrated businesses, such investments may provide considerably higher rates of return. They will however only be made following a favourable external credit assessment and on the specific advice of the Authority's treasury management adviser.

Risk Assessment and Credit Ratings: The Authority uses long-term credit ratings from the three main rating agencies Fitch Ratings, Moody's Investors Service and Standard & Poor's Financial Services to assess the risk of investment default. The lowest available counterparty credit rating will be used to determine credit quality, unless an investment-specific rating is available. Credit ratings are obtained and monitored by the Authority's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made
- any existing investments that can be recalled or sold at no cost will be
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

Where a credit rating agency announces that an 'A-' rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Policy on Use of Financial Derivatives: Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the *Localism Act 2011* removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

The Authority will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

The CLG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Head of Finance, having consulted the Portfolio Holder for Finance, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness.

All Investment activity will be reported in the annual Treasury Management Stewardship Report and supplemented with in-year Treasury Activity Reports to the Audit and Governance Committee.

APPENDIX E

APPORTIONMENT OF INTEREST STRATEGY 2014/15

The Localism Act 2011 required Local Authorities to allocate existing and future borrowing costs between the Housing Revenue Account and the General Fund.

Accordingly, the Authority notionally split its existing debt into General Fund and Housing Revenue Account as detailed in the 'Borrowing Strategy'. Any future borrowing will be assigned in its entirety to the appropriate revenue account.

Interest payable and any other costs arising from long-term loans (for example, premiums and discounts on early redemption) will be charged to the appropriate revenue account.

Interest received on investment income is budgeted to be apportioned between General Fund and the Housing Revenue Account based on an estimated cash flow position. For 2014/15, the budgeted investment income is £68,000 and is apportioned as follows: £43,000 General Fund and £25,000 Housing Revenue Account. Any over or under achievement of investment income is apportioned on this basis, at the end of the financial year.

APPENDIX F

PRUDENTIAL INDICATORS

1 Background

The Local Government Act 2003 requires the Authority to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Authority has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

2. Gross Debt and the Capital Financing Requirement

This is a key indicator of prudence. In order to ensure that over the medium term debt will only be for a capital purpose, the Authority should ensure that the debt does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any additional increases to the capital financing requirement for the current and next two financial years.

The Section 151 Officer reports that the Authority has had no difficulty meeting this requirement in 2012/13, nor is there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3. Estimates of Capital Expenditure

This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax and in the case of the HRA, housing rent levels.

Capital Expenditure	2013/14 Approved £m	2013/14 Revised £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m
Non-HRA	1.779	2.031	2.496	1.122	1.281
HRA	15.865	15.738	14.677	7.558	7.558
Total	**17.644**	**17.769**	**17.173**	**8.680**	**8.839**

Capital expenditure will be financed or funded as follows:

Capital Financing	2013/14 Approved £m	2013/14 Revised £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m
Capital receipts	0.239	0.183	0.529	0.328	0.300
Government Grants	8.873	9.255	8.784	0.224	0.224
Major Repairs Allowance	0.000	3.991	3.991	3.991	3.991
Reserves	3.048	2.635	1.852	0.000	0.017
Other Contribution-s106	0.000	0.055	0.115	0.000	0.000
Grants - Other	0.000	0.000	0.013	0.000	0.000
Revenue contributions	4.213	0.448	0.649	3.388	3.399
Total Financing	16.373	16.567	15.933	7.931	7.931
Supported borrowing	0.000	0.000	0.000	0.000	0.000
Unsupported borrowing	1.271	1.202	1.240	0.749	0.908
Total Funding	1.271	1.202	1.240	0.749	0.908
Total Financing and Funding	**17.644**	**17.769**	**17.173**	**8.680**	**8.839**

4. Ratio of Financing Costs to Net Revenue Stream

This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs. The definition of financing costs is set out in the Prudential Code.

The ratio is based on costs net of investment income.

Ratio of Financing Costs to Net Revenue Stream	2013/14 Approved %	2013/14 Revised %	2014/15 Estimate %	2015/16 Estimate %	2016/17 Estimate %
Non-HRA	10.22	10.08	10.14	9.83	10.18
HRA	14.68	15.87	14.91	14.78	14.65
Total (Average)	**12.95**	**13.59**	**13.31**	**13.21**	**13.25**

5. Capital Financing Requirement

The Capital Financing Requirement (CFR) measures the Authority's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and it's financing.

Capital Financing Requirement	2013/14 Approved £m	2013/14 Revised £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m
Non-HRA	13.619	13.591	14.248	14.421	14.740
HRA	79.155	78.168	77.159	76.128	75.072
Total CFR	**92.774**	**91.759**	**91.407**	**90.549**	**89.812**

6. Actual External Debt

This indicator is obtained directly from the Authority's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities. This Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

Actual External Debt as at 31/03/2013	£m
Borrowing	88.510
Other Long-term Liabilities	0.055
Total	**88.565**

7. Incremental Impact of Capital Investment Decisions

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and Housing Rent levels. The incremental impact is calculated by comparing the total revenue budget requirement of the current approved capital programme with an equivalent calculation of the revenue budget requirement arising from the proposed capital programme.

Incremental Impact of Capital Investment Decisions	2013/14 Approved £	2013/14 Revised £	2014/15 Estimate £	2015/16 Estimate £	2016/17 Estimate £
Increase in Band D Council Tax	2.55	2.59	2.99	2.32	2.63
Increase in Average Weekly Housing Rents	3.76	3.76	4.30	3.40 *	3.29 *

*The Government is proposing to change the basis of the calculation of rents from 2015/16 and has recently consulted on this but the outcome is as yet undetermined. The estimates for 2015/16 and 2016/17 are based on one of four potential options and are therefore subject to change, when a new method has been agreed.

8. Authorised Limit and Operational Boundary for External Debt

The Authority has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise as a consequence of all the financial transactions of the Authority and not just those arising from capital spending reflected in the CFR.

The **Authorised Limit** sets the maximum level of external debt on a gross basis (i.e. excluding investments) for the Authority. It is measured on a daily basis against all external debt items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities). This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases. It is consistent with the Authority's existing commitments, its proposals for capital expenditure and financing and its approved treasury management policy statement and practices.

The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements.

The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

Authorised Limit for External Debt	2013/14 Approved £m	2013/14 Revised £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m
Borrowing	97.100	97.100	99.914	97.579	97.025
Other Long-term Liabilities	1.000	1.000	0.700	0.700	0.700
Total	**98.100**	**98.100**	**100.614**	**98.279**	**97.725**

The Operational Boundary links directly to the Authority's estimates of the CFR and estimates of other cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

The Section 151 Officer has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next meeting of the Council.

Operational Boundary for External Debt	**2013/14 Approved £m**	**2013/14 Revised £m**	**2014/15 Estimate £m**	**2015/16 Estimate £m**	**2016/17 Estimate £m**
Borrowing	95.100	95.100	97.914	95.579	95.025
Other Long-term Liabilities	0.500	0.500	0.500	0.500	0.500
Total	**95.600**	**95.600**	**98.414**	**96.079**	**95.525**

9. Adoption of the CIPFA Treasury Management Code

This indicator demonstrates that the Authority has adopted the principles of best practice.

Adoption of the CIPFA Code of Practice in Treasury Management
The Authority has re-affirmed adoption of the CIPFA Treasury Management Code within this strategy, 11 February 2014.

The Authority has incorporated the changes from the revised CIPFA Code of Practice into its treasury policies, procedures and practices.

10. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

These indicators allow the Authority to manage the extent to which it is exposed to changes in interest rates. The Authority calculates these limits on net principal outstanding sums (i.e. fixed rate debt net of fixed rate investments).

The upper limit for variable rate exposure has been set to ensure that the Authority is not exposed to interest rate rises which could adversely impact on the revenue budget. The limit allows for the use of variable rate debt to offset exposure to changes in short-term rates on investments.

	Existing (Benchmark) level 31/03/13 %	**2013/14 Approved %**	**2013/14 Revised %**	**2014/15 Estimate %**	**2015/16 Estimate %**	**2016/17 Estimate %**
Upper Limit for Fixed Interest Rate Exposure	100	100	100	100	100	100
Upper Limit for Variable Interest Rate Exposure	50	50	50	50	50	50

The limits above provide the necessary flexibility within which decisions will be made for drawing down new loans on a fixed or variable rate basis; the decisions will ultimately be determined by expectations of anticipated interest rate movements as set out in the Authority's treasury management strategy.

Fixed rate investments and borrowings are those where the rate of interest is fixed for the whole financial year. Instruments that mature during the financial year are classed as variable rate.

11. Maturity Structure of Fixed Rate borrowing

This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

It is calculated as the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate. The maturity of borrowing is determined by reference to the earliest date on which the lender can require payment.

Maturity structure of fixed rate borrowing	Lower Limit for 2014/15 %	Upper Limit for 2014/15 %
under 12 months	0	20
12 months and within 24 months	0	20
24 months and within 5 years	0	20
5 years and within 10 years	0	50
10 years and within 20 years	0	50
20 years and within 30 years	0	60
30 years and within 40 years	0	50
40 years and within 50 years	0	50
50 years and above	0	0

12. Upper Limit for total principal sums invested over 364 days

The purpose of this limit is to contain exposure to the possibility of loss that may arise as a result of the Authority having to seek early repayment of the sums invested.

	2013/14 Approved £m	2013/14 Revised £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m
Upper Limit	5	5	5	5	5

APPENDIX G

ANNUAL MINIMUM REVENUE PROVISION STATEMENT

Background

Where the Authority finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP). Although there has been no statutory minimum since 2008, the Local Government Act 2003 requires the Authority to have regard to the Department for Communities and Local Government's Guidance on Minimum Revenue Provision (the Guidance) most recently issued in 2012.

In February 2008 the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [Statutory Instrument 2008/414] were approved by Parliament and became effective on 31 March 2008. These regulations replaced the formula based method for calculating MRP which existed under previous regulations under the Local Government Act 2003. The new regulations required a local authority to determine each financial year an amount of MRP which it considers to be prudent. Linked to this new regulation, the Department of Communities and Local Government (CLG) produced Statutory Guidance which local authorities are required to follow, setting out what constitutes a prudent provision.

The CLG Guidance recommends that before the start of the financial year, a statement of MRP policy for the forthcoming financial year is approved by the Full Council. The broad aim of the Policy is to ensure that MRP is charged over a period that is reasonably commensurate with the period over which the capital expenditure which gave rise to the debt provides benefits. In the case of borrowing supported by Revenue Support Grant, the aim is that MRP is charged over a period reasonably commensurate with the period implicit in the determination of that grant. MRP is not required to be charged to the Housing Revenue Account. Where a local authority's overall CFR is £nil or a negative amount there is no requirement to charge MRP.

The move to International Financial Reporting Standards (IFRS) means that Private Finance Initiative (PFI) schemes and Operating Leases may be brought on Balance Sheet. Where this is the case, such items are classed in accounting terms as a form of borrowing. CLG has therefore proposed amending the Capital Finance Regulations to ensure that the impact on the Revenue account is neutral, with MRP for these items matching the principal repayment embedded within the PFI or lease agreement.

In the case of the Housing Revenue Account (HRA) and following the implementation of the new self-financing arrangements from April 2012, the structure of the debt that was incurred to fund the self-financing was based on the principal being repaid over the life of the HRA business plan, which also takes into account the 'old' HRA debt. For 2014/15, the MRP for HRA is determined by the amounts of principal repaid on the loans that were taken out on an annuity basis.

MRP Options:

Four options for prudent MRP are set out in the CLG Guidance. Details of each are set out below:

<u>Option 1 – Regulatory Method.</u>
MRP under this option, is the amount determined in accordance with the 2003 regulations. In effect, this is 4% of the total Capital Financing Requirement (CFR) excluding HRA borrowing and Adjustment A. Adjustment A is an accounting adjustment to ensure consistency with previous capital regulations. Once calculated this figure is fixed. For this Authority, Adjustment A is fixed at £606,250.49.

Option 2 – CFR Method.

MRP under this option is the same as option 1 but ignores Adjustment A. In effect, this is 4% of the CFR less HRA borrowing.

Option 3 – Asset Life Method.

Where capital expenditure on an asset is financed either wholly or in part by borrowing or credit arrangements, MRP is determined by the life of the asset. For example, if the asset life is 5 years, then the MRP for that asset will be based on 20% of the capital expenditure (unsupported borrowing), per year for 5 years.

Option 4 - Depreciation Method.

Under this option, MRP would be based on the provision required under depreciation accounting. It would also take into account any residual value at the end of the life of the asset. For example, if the asset life was 5 years and the residual value was anticipated to be 10% of the asset value, then the MRP for that asset would be based on 20% of the capital expenditure (unsupported borrowing) less 10% residual value per year for 5 years.

MRP Policy for 2014/15:

The Authority will apply Option 1 in respect of supported capital expenditure.
The Authority will apply Option 2 in respect of unsupported capital expenditure.