STRATEGIC OVERVIEW AND SCRUTINY COMMITTEE

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Agenda Item 6

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SUBMISSION BY CLLR MJ WILCOX, THE LEADER OF THE COUNCIL & THE CABINET MEMBER FOR FINANCE, REVENUES & BENEFITS

Treasury Management Strategy Report 2012-15

1. Purpose of Report

1.1 The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement and Prudential Indicators on an annual basis. This Treasury Management Strategy Statement also incorporates the Annual Investment Strategy that is a requirement of Communities and Local Government's Investment Guidance. Together, these cover the financing and investment strategy for the forthcoming financial year.

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."

1.2 The Council is responsible for its treasury decisions and activity. No treasury management activity is without risk. The successful identification, monitoring and control of risk are an important and integral element of its treasury management activities. The main risks to the Council's treasury activities are:

- Liquidity Risk (Inadequate cash resources)
- Market or Interest Rate Risk (Fluctuations in interest rate levels)
- Inflation Risk (Exposure to inflation)
- Credit and Counterparty Risk (Security of Investments)
- Refinancing Risk (Impact of debt maturing in future years)
- Legal and Regulatory Risk

1.3 The Strategy also takes into account the impact of the Council's Revenue Budget and Capital Programme on the Balance Sheet position, the current and projected Treasury position, the Prudential Indicators and the outlook for interest rates.

1.4 The purpose of this Treasury Management Strategy Statement is, therefore, to approve:

- The Cash Flow forecast for 2012/13 **APPENDIX A**
- Revisions to Treasury Management Strategy and Prudential Indicators for 2011/12.
- Balance Sheet Projections and Borrowing Requirement and Strategy for 2012/13 **APPENDIX B**
- Minimum Revenue Provision Statement 2012/13 – **APPENDIX C**
- Treasury Management Policy Statement and Annual Investment Strategy – **APPENDIX D**
- Use of Specified and Non-Specified Investments – **APPENDICES E & F**
- Prudential Indicators 2012-15 – **APPENDIX G**

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

2. Background

2.1 Cash Flow Forecast

- Treasury Management includes the management of the Council's cash flows as a key responsibility. The planned monthly cash flow forecast for the 2012/13 financial year is shown in detail at **APPENDIX A**. This has been used to calculate the investment income budget and this has been estimated as **£0.126m** (this equates to **3%** of the Council's income from Central Government grant of **£4.135m** in **2012/13**) and interest payments of **£0.013m**.
- The graph of cash flow trends for 2010-13 shows the level of our investments is reducing due to the funding of our Capital Programme and the use of Balances to fund the Revenue Budget.
- In addition, the monthly cash flow together with the graph shows investment levels increase in the first half of the year peaking in September 2012. This is due to receipt of Council Tax and Business Rate income instalments. However, these receipts reduce in the second half of the year because of our spend profile and the Council Tax instalments end in January 2013[1].

2.2 Balance Sheet Projections

- We prepare four year Revenue Forecasts and Capital Programme budgets and these together with the actual Balance Sheet from the previous financial year are used to also prepare 3 year Balance Sheet projections.
- We prepared our accounts in 2010/11 using International Financial Reporting Standards and this meant a number of assets procured using leases and lease type arrangements were included on our Balance Sheet (along with the Finance Lease liabilities). This however also means that when we replace these assets the spend will be treated as capital expenditure and the amount we have estimated in the Capital Programme for finance lease procurements is shown below:

Details	2011/12 Revised £m	2012/13 Original £m	2013/14 Original £m	2014/15 Original £m
Procurements by Finance Lease (vehicles etc)	0.054	0.400	1.076	0

- These Balance Sheet projections (**APPENDIX B**) are key in assessing the Council's Treasury Management Position in terms of borrowing requirement, investment levels and our Investment Policy and Strategy.

2.3 Minimum Revenue Provision Statement 2012/13

- The Council is required to make prudent provision for debt redemption (known as Minimum Revenue Provision or MRP) and each year Council must approve its Minimum Revenue Provision statement and this will include an allowance for leases that appear on the Council's Balance Sheet.
- As in previous years, the Council proposes to base its Minimum Revenue Provision on the life of the asset (**APPENDIX C**).

2.4 Treasury Management Advice and the Expected Movement in Interest Rates

- The interest rate outlook provided by the Council's treasury advisor is shown in the table below:

Official Bank Rate

Projection	Dec 2011	Mar 2012	June 2012	Sept 2012	Dec 2012	Mar 2013	June 2013	Sept 2013	Dec 2013	Mar 2014	Jun 2014	Sep 2014	Dec 2014	Mar 2015
Optimistic[2]						0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central Case	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**

- The Central Case rates have been used as the basis for preparation of the investment income budgets for 2012/13 and future years.

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[1] There is a possibility that the number of Council Tax Payers paying 12 instalments rather than 10 may increase as a result of the Local Government Resource Review (details are shown elsewhere on the agenda for this meeting) and this therefore would impact on the cash flow forecast.

[2] This is in addition to the central case projection.

2.5 Treasury Management Policy Statement, Annual Investment Strategy and Specified and Non Specified Investments

- The criteria and limits for Specified Investments and Non Specified Investments are shown in Detail at **APPENDICES D, E and F**. The changes to those approved in the previous financial year are:

Specified Investments – Money Market Funds (Changes to Limits)

(i) The limit for each individual Money Market Fund is recommended to be reduced from **£2m** to **£1.5m** (to reflect our Treasury Management Advisors recommendation that the limit is reduced from 15% of total investments per fund to 10%).

2.6 Prudential Indicators

The Prudential Indicators are shown in detail at **APPENDIX G**, and in summary in the Financial Implications Section of this Report.

3. Community Benefits

3.1 Management of the Council's resources is essential in order to ensure economical and efficient delivery of Council services.

4. Financial Implications

4.1 The Prudential Indicators are shown in detail at **APPENDIX G** and are summarised below:

PI	Capital expenditure	2011/12 Revised	2012/13 Original	2013/14 Original	2014/15 Original
1	Capital Expenditure (£m)	£5.441m	£5.722m	£2.727m	£0.715m
2	Ratio of Financing Costs to Net Revenue Stream (%)	5%	6%	5%	5%
3	Capital Financing Requirement (£m)	£1.324m	£1.144m	£1.672m	£1.231m
3	Net external borrowing does not exceed the Capital Financing Requirement in the current year plus the next two years (page 9)	True	True	True	True
4	Actual External Debt (£m) includes Finance Leases (page 9)	£1.323m	£1.145m	£1.649m	£1.212m
5	Incremental impact of capital investment decisions on Band D Council Tax (£)	£0.14	£0.14	£0.14	£0.14
6	Authorised limit (£m) (Maximum)	£12.113m	£11.638m	£11.608m	£11.875m
7	Operational boundary (£m) (Maximum)	£2.978m	£2.948m	£2.948m	£2.948m
8	Adoption of CIPFA Code of Practice in Treasury Management	Yes			
9	Net Debt ***(New Indicator)*** (£m)	-£9.658m	-£6.750m	-£3.649m	-£3.571m
	Interest Rate Exposures (%)				
10	Upper Limit for Investments Fixed Interest Rate Exposure	-100%	-100%	-100%	-100%
10	Upper Limit for Investments Variable Interest Rate Exposure	-100%	-100%	-100%	-100%
11	Upper Limit for Borrowings Fixed Interest Rate Exposure	100%	100%	100%	100%
11	Upper Limit for Borrowings Variable Interest Rate Exposure	30%	30%	30%	30%
	Maturity Structure of Fixed Rate Borrowing (Upper Limit) (%)	**Lower Limit**	**Upper Limit**		
12	Under 12 months	0%	100%		
12	12 months and within 24 months	0%	20%		
12	24 months and within 5 years	0%	80%		
12	5 years and within 10 years	0%	40%		
12	10 years and within 20 years	0%	60%		
12	20 years and within 30 years	0%	40%		
12	30 years and within 40 years	0%	40%		
12	40 years and within 50 years	0%	40%		
12	50 years and above	0%	20%		
13	Principal sums invested > 364 days (£m)	£2.10m	£1.90m	£1.30m	£1.20m
14	Credit Risk (***New Indicator***)	We consider security; liquidity and yield, in that order, when making investment decisions.			

5. Risk Management Issues

	Risk Description	Likelihood / Impact	Status	Countermeasure
A	Counterparty default	Medium / High	Financial	Investments are restricted to those organisations with the lowest credit risk: a) The Debt Management Agency Deposit Facility. b) Treasury Bills. c) Money Market Funds with an AAA rating. d) Deposits with other Local Authorities. e) Business Reserve, Term Deposits and Certificates of Deposit with a long term credit rating of A-. As conditions in the Financial Sector improve, we may diversify the counterparty list based on our advisor's recommendations.
B	Adverse Interest Rate fluctuations	Low / Low	Financial	The budget for investment income will be monitored as part of the Council's budget monitoring procedures.
C	Actual cash flows are different to those that are planned	Low / High	Financial	The Council maintains a comprehensive cash flow model that is updated on a daily basis to reflect both actual and planned cash flows. An element of the Council's investment portfolio will be invested in call accounts and Money Market Funds.
D	Planned capital receipts are not received	Medium / High	Financial	The budget for capital receipts will be monitored as part of the Council's budget monitoring procedures.

Background Documents:

CIPFA Code of Practice for Treasury Management in the Public Services

Annual Report on Treasury Management Services and Actual Prudential Indicators 2010/11 Report to Cabinet 6 September 2011

Treasury Management Strategy Report 2011/14 Report to Cabinet 1 February 2011

The Half Year Report on Treasury Management Services and Projected Prudential Indicators 2011/12 Report to Cabinet on 30 November 2011

The Prudential Code for Capital Finance in Local Authorities

Cash Flow Forecast for 2012/13

Investments at 31 December 2011

The table below shows a breakdown of our investments as at the end of the 3rd Quarter using the Lowest acceptable credit rating as a guide to the quality of the investment counterparty.

Counterparty	Principal £m	Matures	Days to Maturity	Rate %	Credit Rating	Foreign Parent
Money Market Funds						
Deutsche Bank	2.0	Instant Access	1	0.72	AAA	N/A
Ignis	2.0	Instant Access	1	0.83	AAA	N/A
Insight	2.0	Instant Access	1	0.77	AAA	N/A
Prime Rate	2.0	Instant Access	1	0.90	AAA	N/A
Other Counterparties						
Santander	2.0	Instant Access	1	0.75	A+	Yes
National Westminster Bank	1.5	Instant Access	1	0.80	A	No
Royal Bank of Scotland	1.0	Instant Access	1	0.80	A	No
Bank of Scotland	1.0	16/04/2012	107	2.05	A	No
Barclays Bank	1.0	13/02/2012	44	1.31	A	No
Barclays Bank	1.0	20/06/2012	172	1.47	A	No
Lloyds TSB	2.0	18/07/2012	200	2.05	A	No
Nationwide	2.0	23/01/2012	23	1.02	A	No
Midlothian Council	1.0	15/02/2012	46	0.38	AAA	N/A
Fife Council	1.0	24/02/2012	55	0.35	AAA	N/A
Total	**£21.5**					

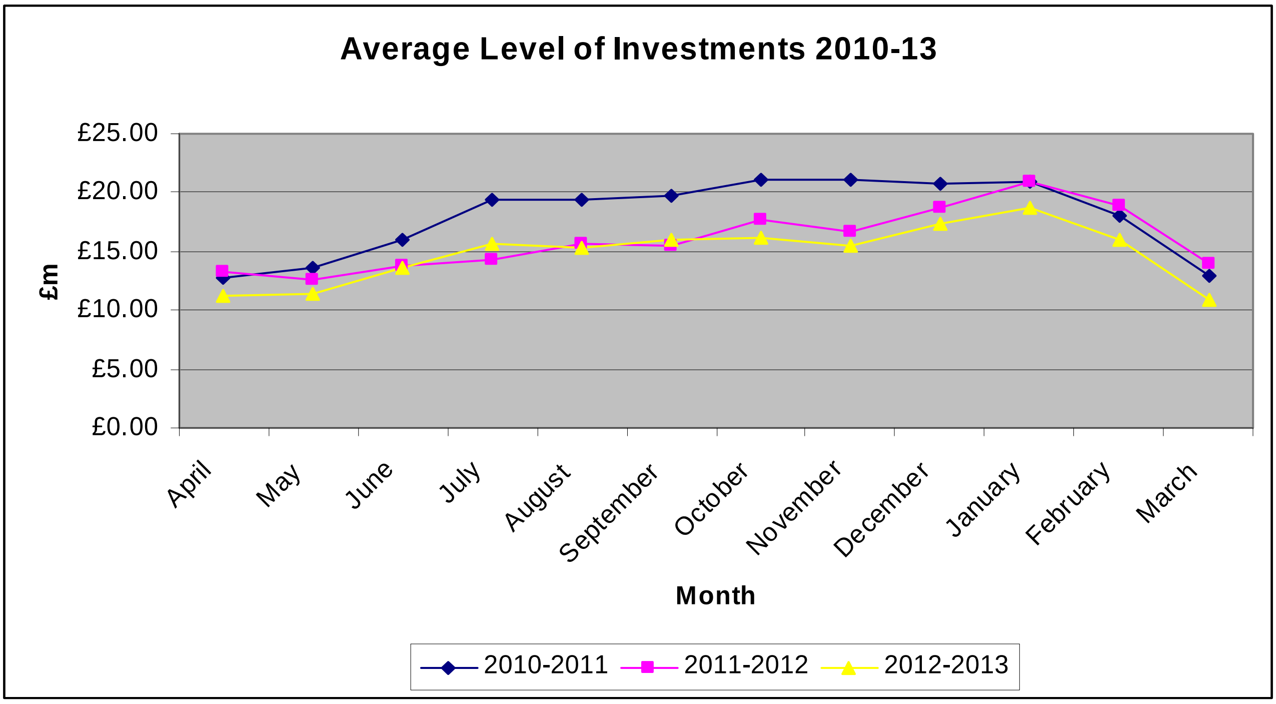
The aim for the risk status of our portfolio is **A-** or a higher credit rating. This reflects our current investment approach with the main focus on security and the safe return of our investments. Our risk rating at 31st December 2011 had a more secure risk status of **A+** based on the length of the investment and **AA** based on the value of the investment.

Detailed Cash flow for 2012/13

	2012/13 (£m)												
Detail	**April**	**May**	**June**	**July**	**Aug**	**Sept**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**Total**
Income													
Council Tax and NNDR Income	-8.37	-7.75	-7.66	-7.56	-8.27	-7.76	-7.47	-7.47	-7.47	-7.47	-1.65	-1.03	-79.93
Benefit Grant	-1.97	-1.97	-2.59	-1.98	-1.97	-1.97	-1.45	-1.81	-1.81	-1.81	-1.81	-1.85	-22.99
Net Revenue Income	0.13	-0.27	-0.27	-0.27	-0.27	-0.27	-0.27	-0.27	-0.27	-0.27	-0.25	-0.34	-2.89
Revenue Grant	-0.79	-0.36	-0.36	-0.36	-0.36	-0.36	-0.36	-0.36	-0.36	-0.36	-0.38	-0.29	-4.70
Capital Income	-0.03	-0.03	-0.03	-0.03	-0.03	-2.36	-0.03	-0.03	-0.03	-0.03	-0.03	-0.06	-2.72
Expenditure													
Capital Spend	0.44	0.44	0.44	0.44	0.44	0.44	0.44	0.44	0.44	0.44	0.44	0.43	5.27
Benefit Payments	1.09	1.37	1.63	1.59	1.49	1.60	1.17	1.09	1.09	1.90	1.09	1.10	16.21
Employees	1.22	1.17	1.22	1.16	1.20	1.22	1.20	1.26	1.32	1.28	1.28	1.31	14.84
NNDR Pool	2.10	2.84	2.84	2.84	2.84	2.84	2.84	2.84	2.84	2.84	0.60	1.65	29.91
Precepts	6.00	4.86	0	4.86	4.86	5.19	4.86	4.86	0	4.86	4.86	4.86	50.07
CASHFLOW	-0.18	0.30	-4.78	0.69	-0.07	-1.43	0.93	0.55	-4.25	1.38	4.15	5.78	3.07
Average level of investments	11.06	11.00	13.25	15.30	15.00	15.75	16.00	15.28	17.15	18.60	15.86	10.84	

Average Level of Investments 2010-13

The graph below shows the actual trend of average investment levels in 2010/11 together with projected levels for 2011/12 and 2012/13. The level of our investments is reducing due to the use of reserves to support our Revenue Budget together with the funding of our Capital Programme.



Investment Income and Borrowing Cost Budgets for 2012/13

Based on the cash flow forecast on the previous page, the estimate for interest payments in 2012/13 is **£0.013m** and for interest receipts is **£0.126m**.

In terms of interest receipts, there are two key risks / sensitivities:

a) The interest rate receivable.
b) The amount of money we have available to invest.

What if

Interest Rates Change	We have more cash available to invest £000s				
	+£1m	**+£2m**	**+£3m**	**+£4m**	**+£5m**
Current Estimate	134	143	151	160	168
+0.50%	213	227	240	254	267

Balance Sheet Projections 2012-15

Balance	31 Mar 2011 Actual £m	31 Mar 2012 Estimate £m	31 Mar 2013 Estimate £m	31 Mar 2014 Estimate £m	31 Mar 2015 Estimate £m
Non Current Assets					
1. Property, Plant and Equipment, Investment Property & Intangible Assets	50.649	48.747	50.491	51.014	49.732
4. Long Term Debtors	0.236	0.215	0.186	0.162	0.156
Current Assets					
4. Current Assets (including accrued interest)	5.797	5.797	5.797	5.797	5.797
2. Short Term Investments (excluding accrued interest)	7.448	9.669	6.728	5.298	4.783
2. Cash and Cash Equivalents	2.846				
Current Liabilities					
3. Short Term Borrowing	-0.005	-0.005	-0.030	0	0
3. Finance Leases	-0.523	-0.568	-0.536	-0.431	-0.531
4. Short Term Creditors	-7.046	-7.046	-7.046	-7.046	-7.046
4. Receipts in Advance	-0.247	-0.090	0	0	0
Long Term Liabilities					
3. Finance Leases	-1.240	-0.720	-0.579	-1.218	-0.681
3. Borrowing	-0.035	-0.030	0	0	0
4. Pension Scheme	-20.187	-20.187	-20.187	-20.187	-20.187
4. Receipts in Advance	-0.863	-0.279	0	0	0
Total Assets less Liabilities	**36.830**	**35.503**	**34.824**	**33.389**	**32.023**

Usable Reserves					
4. Capital Grants Unapplied	-1.636	-0.882	-0.009	-0.009	-0.009
5. Usable Capital Receipts***	-2.087	-1.677	-0.571	-0.139	-0.129
5. Burntwood Leisure Centre Sinking Fund	-0.665	-0.456	-0.305	-0.011	-0.011
5. Burntwood Synthetic Pitch Sinking Fund	-0.029	-0.029	0	0	0
5. City Centre Redevelopment Sinking Fund	-0.024	-0.024	-0.024	-0.024	-0.024
5. King Edwards Leisure Centre Sinking Fund	-0.031	-0.031	0	0	0
5. Lombard Street Car Park Sinking Fund	-0.017	-0.017	-0.017	-0.017	-0.017
5. Elections	-0.095	-0.095	-0.095	-0.095	-0.095
5. Public Open Spaces	-0.007	-0.007	-0.007	-0.007	-0.007
5. Three Spires Multi Storey Reserve	-0.994	-1.141	-1.271	-1.109	-1.264
5. Earmarked Reserves	-1.413	-1.353	-1.353	-1.353	-1.353
5. Grant Aid	-0.038	-0.038	-0.038	-0.038	-0.038
5. Building Regulations	-0.006	-0.006	-0.006	-0.006	-0.006
5. General Fund Balance	-3.406	-2.749	-2.209	-1.669	-1.000
Unusable Reserves					
1. Revaluation Reserve	-4.932	-4.932	-4.932	-4.932	-4.932
1. Capital Adjustment Account	-41.873	-42.491	-44.414	-44.410	-43.569
4. Deferred Credits	-0.011	-0.009	-0.007	-0.004	-0.003
4. Benefits Payable during Employment	0.233	0.233	0.233	0.233	0.233
5. Collection fund	0.014	0.014	0.014	0.014	0.014
4. Pension Scheme	20.187	20.187	20.187	20.187	20.187
Total Equity	**-36.830**	**-35.503**	**-34.824**	**-33.389**	**-32.023**

*** - Assumes receipt of **£2.3m** in relation to the Friarsgate Garage in September 2012.

Borrowing Requirement and Strategy

We finance our capital spend from a variety of sources including capital receipts, revenue and grants and contributions. Any capital spend we do not fund from these sources increases our underlying need to borrow for capital purposes (the Capital Financing Requirement (CFR)).

The Capital Financing Requirement together with the level of our Balances and Reserves (B&R) are the core drivers of Treasury Management Activity. A summary of our Balance Sheet Projections detailed on the previous page showing the estimated level of our Capital Financing Requirement, Investments, Long Term Borrowing and Finance Leases, Net Creditors and Balances and Reserves is provided in the table below:

31 Mar 2011 Actual £m	Details	31 Mar 2012 Estimate £m	31 Mar 2013 Estimate £m	31 Mar 2014 Estimate £m	31 Mar 2015 Estimate £m
3.844	1. Capital Financing Requirement	1.324	1.145	1.673	1.232
10.294	2. Investments	9.669	6.728	5.298	4.783
-1.803	3. Long Term Borrowing and Finance Leases	-1.323	-1.145	-1.649	-1.212
-3.537	4. Net Creditors	-2.061	-0.846	-0.868	-0.872
-8.798	5. Balances and Reserves	-7.609	--5.882	-4.454	-3.931

*** - Assumes receipt of **£2.3m** in relation to the Friarsgate Garage in September 2012.

We can use the capital financing related elements of these projections to assess when the Council would need to borrow to fund its Capital Programme, and these estimates are shown in the table below:

31 Mar 2011 Actual £m	Details	31 Mar 2012 Estimate £m	31 Mar 2013 Estimate £m	31 Mar 2014 Estimate £m	31 Mar 2015 Estimate £m
3.844	The amount of our capital spend that is not financed from capital receipts, revenue, grants and contributions (known as the Capital Financing Requirement)	1.324	1.145	1.673	1.232
-1.803	Less: current funding provided through finance leases and long term borrowing	-1.323	-1.145	-1.649	-1.212
2.041	**Projected Borrowing Need**	**0.001**	**0**	**0.024**	**0.020**
-8.798	Less: the projected level of our balances and reserves we currently hold as investments	-7.609	-5.882	-4.454	-3.931
-6.757	**Our net projected borrowing need (a positive figure indicates when we need to borrow)**	**-7.608**	**-5.882**	**-4.430**	**-3.911**

What If	Our balances and reserves are £0.5m lower and the Friarsgate Garage reimbursement is received a year later than planned	**-7.108**	**-3.082**	**-3.930**	**-3.411**
	Our balances and reserves are £1m lower and the Friarsgate Garage reimbursement is received two years later than planned	**-6.608**	**-2.582**	**-1.130**	**-2.911**

Minimum Revenue Provision Statement 2012/13

The level of our Capital Financing Requirement measures our underlying need to borrow for a capital purpose. To ensure that this expenditure will ultimately be financed, we are required to make a Minimum Revenue Provision for Debt Redemption (MRP) from within the Revenue budget each year. Capital Expenditure that is not financed from capital receipts, revenue or grants and contributions will increase the Capital Financing Requirement and this will in turn produce an increased requirement to charge Minimum Revenue Provision in the Revenue Account.

The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (Statutory Instrument 2008/414) place a duty on local authorities to make a prudent provision for debt redemption. The Secretary of State has issued guidance on Minimum Revenue Provision and local authorities are required to “have regard” to such Guidance under Section 21(1A) of the Local Government Act 2003.

The four Minimum Revenue Provision options available are:

Option 1: Regulatory Method
Option 2: Capital Financing Requirement Method
Option 3: Asset Life Method
Option 4: Depreciation Method

The changes due to the 2009 Statement of Recommended Practice and International Financial Reporting Standards have resulted in new assets and leases being brought onto the Balance Sheet. Therefore, the Capital Financing Requirement has increased, and has lead to an increase in the Minimum Revenue Provision charge to revenue. Minimum Revenue Provision for these items will match the annual principal repayment for the associated deferred liability.

Minimum Revenue Provision in 2012/13: Options 1 and 2 may be used only for supported expenditure (where the Government provides financial support to offset the borrowing costs through the Revenue Support Grant mechanism). Methods of making prudent provision for self financed expenditure include Options 3 and 4 (which may also be used for supported expenditure if the Council chooses).

The Minimum Revenue Provision Statement will be submitted to Council before the start of the 2012/13 financial year. If it is ever proposed to vary the terms of the original Minimum Revenue Provision Statement during the year, a revised statement should be put to Council at that time.

The Council will apply Option 3 in respect of supported and unsupported capital expenditure and Minimum Revenue Provision in respect of leases brought on Balance Sheet and will match the annual principal repayment for the associated Finance Lease liability.

Treasury Management Policy Statement

Introduction and Background

The Council adopts the key recommendations of Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services: Code of Practice (the Code), as described in Section 5 of the Code.

Accordingly, the Council will create and maintain, as the cornerstones for effective treasury management:-

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

- Suitable treasury management practices (TMPs), 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.

The Council (i.e. full 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 (this Report), a mid-year review and an annual report after its close, in the form prescribed in its Treasury Management Practices.

The Council delegates responsibility for the implementation and monitoring of its treasury management policies and practices to Cabinet and for the execution and administration of treasury management decisions to the Director of Finance, Revenues & Benefits, who will act in accordance with the organisation's policy statement and Treasury Management Practices and Chartered Institute of Public Finance and Accountancy's (CIPFA) Standard of Professional Practice on Treasury Management.

The Council nominates Strategic (Overview and Scrutiny) Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

Policies and Objectives of Treasury Management Activities

The Council defines its treasury management activities as:

"The management of the Council'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."

This Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

This Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable performance measurement.

The Council currently does not plan to borrow to fund its capital expenditure. However, should this situation change and Council approve borrowing for a capital purpose, the Council's borrowing will be affordable, sustainable and prudent and consideration will be given to the management of interest rate risk and refinancing risk. The source from which the borrowing is taken and the type of borrowing should allow the Council transparency and control over its debt.

The Council's primary objective in relation to investments remains the security of capital. The liquidity or accessibility of the Authority's investments followed by the yield earned on investments remain important but are secondary considerations.

Annual Investment Strategy

Background

Guidance from Communities and Local Government (CLG) on Local Government Investments in England requires that an Annual Investment Strategy (AIS) be set. In accordance with Investment Guidance issued by the CLG and best practice this Authority's primary objective in relation to the investment of public funds remains the **security of capital**. The liquidity or accessibility of the Authority's investments followed by the yields earned on investments is important but are secondary considerations[3].

The CLG Investment Guidance states that a specified investment is one made with a body or scheme of "high credit quality". Non Specified Investments are, effectively, everything else.

We will continue to maintain a counterparty list based on these criteria and will monitor and update the credit standing of the institutions on a regular basis. This assessment will include credit ratings and other alternative assessments of credit strength such as:

- Credit Default Swaps (where quoted)
- Share Price (where quoted)
- Gross Domestic Product (GDP); Net debt as a Percentage of Gross Domestic Product.
- Sovereign Support Mechanisms / Potential Support from well resourced parent institutions.
- Macro economic indicators
- Corporate developments and information in the general and financial media

Maximum Periods for which Funds can be Committed

The maximum sums that could be invested for a period of greater than 364 days are based on our Balance Sheet position with the limit being set in Prudential Indicator 13 – Upper Limit for total principal sums invested over 364 days.

Borrowing in Advance of Need[4]

We currently do not plan to borrow on a long term basis to fund capital expenditure and therefore there are no plans to borrow in advance of capital spend.

Investments managed in-house

Our investments are made with reference to our cash flow forecast shown at **APPENDIX A** and the level of projected interest rates shown at Section 3.4. In any period of significant stress in the markets, the default position is for investments to be made with the Debt Management Office.

Currently the Council has restricted its investment activity to:

- The Debt Management Agency Deposit Facility (The rates of interest from the DMADF are below equivalent money market rates. However, the returns are an acceptable trade-off for the guarantee that the Council's capital is secure)
- AAA-rated Money Market Funds with a Constant Net Asset Value (CNAV)
- Deposits with other local authorities
- Treasury Bills
- Business reserve accounts and term deposits. *These have been primarily restricted to UK institutions that are considered systemically important.*

However, this report recommends some changes to its Specified Investments and their Limits. Specified Investments are set out in **APPENDIX E.**

[3] The speculative procedure of borrowing purely in order to invest is unlawful.
[4] This is a practice where you borrow early and then invest the money until the capital spend takes place.

The Director of Finance, Revenues and Benefits, 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. Decisions taken on the core investment portfolio will be reported to future Cabinet meetings.

The Use of Financial Instruments for the Management of Risks

Currently, Local Authorities' legal power to use derivative instruments remains unclear. The General Power of Competence enshrined in the Localism Bill is not sufficiently explicit. Consequently, the authority does not intend to use derivatives. Should this position change, we may seek to develop a detailed and robust risk management framework governing the use of derivatives, but this change in strategy will require full Council approval.

Balanced Budget Requirement

We comply with the provisions of Section 32 of the Local Government Finance Act 1992 to set a Balanced Budget.

Monitoring and Reporting on the Treasury Outturn and Prudential Indicators

Treasury activity is monitored daily and reported internally to the Financial Services Manager. The Financial Services Manager will monitor the Prudential Indicators through the year. The Director of Finance, Revenues and Benefits will report to the Cabinet on treasury management activity / performance as follows:

(a) Quarterly investment and borrowing activity as part of the Performance against the Financial Strategy.
(b) Half yearly against the Treasury Management Strategy approved for the year.
(c) An outturn report on its treasury activity no later than 30th September after the financial year-end.

In addition, Strategic (Overview and Scrutiny) Committee will be responsible for the Scrutiny of treasury management activity and practices.

Member Training

Our approach is:

- To identify Members who require training.
- To assess the level of training required and to procure training from an external organisation with expertise in this area.
- To monitor the ongoing training needs of Members based on legislative, regulatory and best practice requirements.

As part of the ongoing training approach which included training all new Members, we invited all Members to a training event on 27th July 2011 in relation to the principles of Treasury Management.

Investment Consultants

Our approach to the use of investment consultants is:

- To use external advisors to provide advice and guidance in relation to the areas covered within the Treasury Management Strategy Statement such as capital spend and funding, Balance Sheet projections, Prudential Indicators, Investment Guidance and assistance in assessing the impact of Legislative and Regulatory changes on the Council's budgets and policies.
- The quality of this service is controlled through a regular market testing exercise (recently undertaken in June 2009 and due to be undertaken in June 2012) and through regular meetings with the advisors.

Publication

Our Treasury Management Statement is published on the Council's website.

Use of Specified and Non Specified Investments

Specified Investments identified for use by the Council

Specified Investments will be those that meet the criteria in the CLG Guidance, i.e. the investment

- is sterling denominated
- has a maximum maturity of 1 year
- meets the "high" credit criteria as determined by the Council or is made with the UK government or is made with a Local Authority in England, Wales and Scotland.
- the making of which is not defined as Capital Expenditure under Section 25(1)(d) in SI 2003 No 3146 (i.e. the investment is not loan capital or share capital in a body corporate).

"Specified" Investments identified for the Council's use are:

- Deposits in the Debt Management Office's (DMO) Debt Management Account Deposit Facility
- Treasury Bills
- Deposits with UK local authorities
- Deposits in term investments or certificates of deposit with banks and building societies
- AAA-rated Money Market Funds (MMF) with a Constant Net Asset Value (CNAV)

For credit rated Bank and Building Society counterparties, the minimum criteria will be the short-term/long-term ratings assigned by various agencies which may include Moody's Investors Services, Standard & Poor's, Fitch Ratings.

Agency	***Minimum Long Term Rating***	***Minimum Short Term Rating***
Fitch	*A-*	*F1*
Moody's	*A3*	*P-1*
Standard and Poors (S&P)	*A-*	*A-1*

For Money Market Fund counterparties, the highest rating assigned by the agency of Constant Net Asset Value (CNAV) funds is:

Agency	***Highest Rating***
Fitch	*AAAmmf (this is Fitch's revised rating scale and corresponds to the Agency's previous AAA/V1+ rating)*
Moody's	*Aaa/MR1+*
Standard and Poors (S&P)	*AAAm*

The Council will also take into account information on corporate developments and market sentiment towards investment counterparties.

Within the categories above, and in accordance with the Code, the Council has developed additional criteria to set the overall amount of monies, which will be invested in these bodies. This criteria is:

- No more than **£3m** (Current Limit is **£3m**) with one counterparty, including any subsidiaries, at the time the investment is undertaken known as the "group limit".
- The Sovereign Limit for the UK will be **100%**. At present we do not plan to make any investments with Non UK banks and Building Societies.

New specified investments will be made within the following limits (and subject to our Treasury Management Advisors guidance):

Instrument	**Country**	**Counterparty**	**Current Limit £m**	**Recommended Limit £m**
Term Deposits	UK	Debt Management Account Deposit Facility (DMADF), Debt Management Office (DMO)	No limit	No limit
Treasury Bills	UK	Debt Management Office (DMO)	No Limit	No Limit
Term Deposits	UK	Other UK Local Authorities	No limit	No limit
Term Deposits / Certificates of Deposit / Call Accounts	UK	Santander UK Plc	£2m	£2m
Term Deposits / Certificates of Deposit / Call Accounts	UK	Bank of Scotland/Lloyds	£2m	£2m
Term Deposits / Certificates of Deposit / Call Accounts	UK	Barclays	£2m	£2m
Term Deposits / Certificates of Deposit / Call Accounts	UK	Clydesdale	£2m	£2m
Term Deposits / Certificates of Deposit / Call Accounts	UK	HSBC	£2m	£2m
Term Deposits / Certificates of Deposit / Call Accounts	UK	Nationwide	£2m	£2m
Term Deposits / Certificates of Deposit / Call Accounts	UK	Royal Bank of Scotland	£2m	£2m
Term Deposits / Certificates of Deposit / Call Accounts	UK	National Westminster Bank	£2m	£2m
Term Deposits / Certificates of Deposit / Call Accounts	UK	Standard Chartered Bank	£2m	£2m
AAA rated Money Market Funds (each Fund)	UK/Ireland/ Luxembourg	CNAV MMFs	£2m	£1.5m

Authority's Banker – The Authority banks with National Westminster Bank. At the current time, it does meet the minimum credit criteria of A- (or equivalent) long term. However, Even if the credit rating falls below the Authority's minimum criteria National Westminster Bank will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

Non-Specified Investments determined for use by the Council

Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the Council's use:

	Maximum maturity[5]	Current Limit £m	Recommended Limit £m
▪ Deposits with banks and building societies ▪ Certificates of deposit with banks and building societies	2 yrs	£2.1m	£1.9m

For credit rated counterparties, the minimum criteria will be the short-term / long-term ratings assigned by various agencies which may include Moody's Investors Services, Standard & Poor's, Fitch Ratings for investments between 1 and 2 years are:

Agency	***Minimum Long Term Rating***	***Minimum Short Term Rating***
Fitch	*A+*	*F1*
Moody's	*A1*	*P-1*
Standard and Poors (S&P)	*A+*	*A-1*

Within the categories above, and in accordance with the Code, the Council has developed additional criteria to set the overall amount of monies, which will be invested in these bodies. These criteria are:

- No more than **£3m** (Current Limit is £3m) with one counterparty, including any subsidiaries, at the time the investment is undertaken known as the "group limit".
- The Sovereign Limit for the UK will be **100%.** At present we do not plan to make any investments with Non UK banks and Building Societies.

[5] In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty.

PRUDENTIAL INDICATORS 2012-15

1 Background:

There is a requirement under the Local Government Act 2003 for Local Authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators.

2. Net Borrowing and the Capital Financing Requirement:

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

The Director of Finance, Revenues and Benefits reports that the Authority had no difficulty meeting this requirement in 2011/12, and there are no 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:

3.1 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.

No. 1 Capital Financing	**2011/12 Original £m**	**2011/12 Approved[6] £m**	**2011/12 Revised £m**	**2012/13 Original £m**	**2013/14 Original £m**	**2014/15 Original £m**
Non Current Assets	1.885	2.335	2.944	3.526	2.082	0.200
Capital Expenditure Funded from Revenue under Statute	1.498	2.668	2.497	2.196	0.645	0.515
Total	**£3.383m**	**£5.003m**	**£5.441m**	**£5.722m**	**£2.727m**	**£0.715m**

3.2 Capital expenditure will be financed as follows:

No. 1 Capital Financing	**2011/12 Original £m**	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Original £m**	**2013/14 Original £m**	**2014/15 Original £m**
Capital receipts	0.996	1.209	1.687	3.406	0.432	0.010
Burntwood Sinking Fund	0.112	0.210	0.209	0.151	0.294	0
Other Sinking Funds	0	0	0	0.060	0	0
Capital Grants and Contributions	2.161	3.440	3.392	1.679	0.331	0.327
Earmarked Reserves	0	0.060	0.069	0.026	0.319	0
Revenue contributions	0.060	0.030	0.030	0	0.275	0.378
Supported borrowing	0	0	0	0	0	0
Finance Leases	0.054	0.054	0.054	0.400	1.076	0
Total	**£3.383m**	**£5.003m**	**£5.441m**	**£5.722m**	**£2.727m**	**£0.715m**

Note: the element to be financed from borrowing and finance leases impacts on the movement in the Capital Financing Requirement.

[6] Approved Budget at the half year.

4. Ratio of Financing Costs to Net Revenue Stream:

4.1 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 borrowing costs. The definition of financing costs id set out in the Prudential Code.

4.2 The ratio is based on costs net of investment income (where investment income exceeds the costs of borrowing, the indicator will be negative).

No. 2 Ratio of Financing Costs to Net Revenue Stream	**2011/12 Original %**	**2011/12 Approved %**	**2011/12 Revised %**	**2012/13 Original %**	**2013/14 Original %**	**2014/15 Original %**
Non-HRA	0	4	5	6	5	5
Total	**0%**	**4%**	**5%**	**6%**	**5%**	**5%**

5. Capital Financing Requirement:

5.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. The calculation of the Capital Financing Requirement is taken from the amounts held in the Balance Sheet relating to capital expenditure and it's financing. It is an aggregation of the amounts shown for Non Current Assets, the Revaluation Reserve, the Capital Adjustment Account and any other balances treated as capital expenditure.

No. 3 Capital Financing Requirement	**2011/12 Original £m**	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Original £m**	**2013/14 Original £m**	**2014/15 Original £m**
Non-HRA	1.097	1.324	1.324	1.144	1.672	1.231
Total	**£1.097m**	**£1.324m**	**£1.324m**	**£1.144m**	**£1.672m**	**£1.231m**

5.2 The year–on-year change in the Capital Financing Requirement is due to the following:

No. 3 Capital Financing Requirement	**2011/12 Original £m**	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Original £m**	**2013/14 Original £m**	**2014/15 Original £m**
Balance Brought Forward	**1.501**	**3.844**	**3.844**	**1.324**	**1.144**	**1.672**
Capital expenditure financed from finance leases or borrowing (per 3.2)	0.054	0.054	0.054	0.400	1.076	0
Reimbursement of Chasewater Dam Spend not financed in previous years	0	-2.053	-2.053	0	0	0
Revenue provision for debt Redemption.	-0.458	-0.521	-0.521	-0.580	-0.548	-0.441
Balance Carried Forward	**£1.097m**	**£1.324m**	**£1.324m**	**£1.144m**	**£1.672m**	**£1.231m**

6. Actual External Debt (see also page 9 for projections):

6.1 This indicator is obtained directly from the Council'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.

No. 4	**Actual External Debt as at 31/03/2011**	**£m**
	Borrowing – Long Term Element	0.035
	Borrowing – Short Term Element	0.005
	Other Long-term Liabilities (Finance Leases)	1.242
	Short-term Liabilities (Finance Leases)	0.521
	Total	**£1.803m**

7. Incremental Impact of Capital Investment Decisions:

7.1 This is an indicator of affordability that shows the impact of Capital investment decisions on Council Tax 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.

No. 5 Incremental Impact of Capital Investment Decisions	**2011/12 Original £**	**2011/12 Approved £**	**2011/12 Revised £**	**2012/13 Original £**	**2013/14 Original £**	**2014/15 Original £**
Increase in Band D Council Tax	£0.21	£0.14	£0.14	£0.14	£0.14	£0.14

7.2 The estimate of procurements made by Finance Leases which are included in the Capital Programme mainly for the replacement of current assets is shown in the table below:

	2011/12 Original £m	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Original £m**	**2013/14 Original £m**	**2014/15 Original £m**
New Vehicle and Plant Procurements	£0.054m	£0.054m	£0.054m	£0.400m	£1.076m	£0m

8. Authorised Limit and Operational Boundary for External Debt:

8.1 The Council 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 Council and not just those arising from capital spending reflected in the Capital Financing Requirement.

8.2 The **Authorised Limit** sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external-borrowing 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 Council's existing commitments, its proposals for capital expenditure and financing and its approved Treasury Management Policy statement and practices.

8.3 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.

8.4 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).

No. 6 Authorised Limit for External Debt	**2011/12 Original £m**	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Original £m**	**2013/14 Original £m**	**2014/15 Original £m**
Borrowing	7.665	7.665	7.665	7.190	7.160	7.427
Other Long-term Liabilities	4.448	4.448	4.448	4.448	4.448	4.448
Total	**£12.113m**	**£12.113m**	**£12.113m**	**£11.638m**	**£11.608m**	**£11.875m**

8.5 The **Operational Boundary** links directly to the Council's estimates of the Capital Financing Requirement and estimates of other cashflow 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.

8.6 The Director of Finance, Revenues and Benefits 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 Full Council.

No. 7 Operational Boundary for External	**2011/12 Original £m**	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Original £m**	**2013/14 Original £m**	**2014/15 Original £m**
Borrowing	0.533	0.533	0.530	0.500	0.500	0.500
Other Long-term Liabilities	2.448	2.448	2.448	2.448	2.448	2.448
Total	**£2.981m**	**£2.981m**	**£2.978m**	**£2.948m**	**£2.948m**	**£2.948m**

9 Adoption of the CIPFA Treasury Management Code:

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

No. 8	**Adoption of the CIPFA Code of Practice in Treasury Management**
	The Council approved the adoption of the CIPFA Treasury Management Code at its Full Council meeting on 25th February 2003. The Council has incorporated any changes resulting from the revisions to the CIPFA Treasury Management Code within its treasury policies, practices and procedures.

10. Gross and Net Debt (*New Prudential Indicator*)

10.1 The purpose of this treasury indicator is to highlight a situation where the Council is planning to borrow in advance of need.

No. 9 Gross and Net Debt	**2011/12 Original £m**	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Original £m**	**2013/14 Original £m**	**2014/15 Original £m**
Outstanding Borrowing (at nominal value)	**New**	**New**	0.035	0.030	0	0
Other Long-term Liabilities (at nominal value)			1.288	1.115	1.649	1.212
Gross Debt			**1.323**	**1.145**	**1.649**	**1.212**
Less : Investments			-10.981	-7.895	-5.298	-4.783
Net Debt			**-9.658**	**-6.750**	**-3.649**	**-3.571**

11. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure:

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

11.2 The upper limit for variable rate exposure has been set to ensure that the Council is not exposed to interest rate rises, which could adversely impact on the revenue budget.

No.	**Interest Rate Exposures**	**2011/12 Original %**	**2011/12 Approved %**	**2011/12 Revised %**	**2012/13 Original %**	**2013/14 Original %**	**2014/15 Original %**
Fixed Interest Rates							
10	Upper Limit for Fixed Interest Rate Exposure on Investments	-100	-100	-100	-100	-100	-100
	Upper Limit for Fixed Interest Rate Exposure on Debt	100	100	100	100	100	100
Net Fixed Exposure		**0%**	**0%**	**0%**	**0%**	**0%**	**0%**
Variable Interest Rates							
11	Upper Limit for Variable Rate Exposure on investments	-75	-100	-100	-100	-100	-100
	Upper Limit for Variable Interest Rate Exposure on Debt	30	30	30	30	30	30
Net Variable Exposure		-45%	-70%	-70%	-70%	-70%	-70%

12. Maturity Structure of Fixed Rate borrowing:

12.1 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.

12.2 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.

No. 12	Maturity structure of fixed rate borrowing	Existing Level at 31st March 2011 (%)	Lower Limit %	Upper Limit %
	Under 12 months	13	0	100[7]
	12 months and within 24 months	13	0	20
	24 months and within 5 years	75	0	80
	5 years and within 10 years	0	0	40
	10 years and within 20 years	0	0	60
	20 years and within 30 years	0	0	40
	30 years and within 40 years	0	0	40
	40 years and within 50 years	0	0	40
	50 years and above	0	0	20

13. Upper Limit for total principal sums invested over 364 days:

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

No. 13 Upper Limit for total principal sums invested over 364 days	2011/12 Original £m	2011/12 Approved £m	2011/12 Revised £m	2012/13 Original £m	2013/14 Original £m	2014/15 Original £m
	£2.10m	£2.10m	£2.10m	£1.90m	£1.30m	£1.20m

14. Credit Risk (new Prudential Indicator):

14.1 We consider security, liquidity and yield, in that order, when making investment decisions.

14.2 Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in our assessment of counterparty credit risk.

14.3 We also consider alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution (minimum A- or equivalent);
- Sovereign support mechanisms;
- Credit default swaps (where quoted);
- Share prices (where available);
- Economic fundamentals, such as a country's net debt as a percentage of its GDP);
- Corporate developments, news, articles, markets sentiment and momentum;
- Subjective overlay.

14.4 The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

[7] This will include any short term fixed rate borrowing we need to undertake for cash flow purposes.