STRATEGIC OVERVIEW AND SCRUTINY COMMITTEE

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Agenda Item : 7

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SUBMISSION BY CLLR MJ WILCOX, THE LEADER OF THE COUNCIL & THE PORTFOLIO HOLDER FOR FINANCE, REVENUES & BENEFITS

Annual Report on Treasury Management Services and Actual Prudential Indicators 2011/12

1. Purpose of Report

Background

1.1 The Annual Treasury Report is a requirement of the Council's reporting procedures. It covers the Treasury activity during 2011/12 and the actual Prudential Indicators for 2011/12.

1.2 Our treasury management activity is underpinned by CIPFA's Code of Practice on Treasury Management ("the Code"), which requires local authorities to produce annually Prudential Indicators and a Treasury Management Strategy Statement on the likely financing and investment activity. The Code also recommends that members be informed of treasury management activities at least twice a year. We report quarterly to the Cabinet and scrutiny on treasury policy, strategy and activity is delegated to the Strategic (Overview and Scrutiny) Committee.

1.3 Treasury management is defined as: "The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.4 Overall responsibility for treasury management remains with the Council. No treasury management activity is without risk; the effective identification and management of risk are integral to our treasury management objectives.

Scope

1.5 This report is prepared in accordance with the revised CIPFA Treasury Management Code and the revised Prudential code and;

a) presents details of capital spend, capital financing, borrowing and investment transactions;
b) reports on the risk implications of treasury decisions and transactions;
c) gives details of the outturn position on treasury management transactions in 2011/12;
d) confirms compliance with treasury limits and Prudential Indicators and
e) provides details of the results of recent reviews undertaken in relation to Treasury Management Activity to provide assurance that systems and controls work as expected.

1.6 The report is to full Council and is in addition also being submitted to Cabinet who are responsible for the Treasury Management function.

2. Background

2.1 Interest Rates and Investment Strategy

- Our interest rate projections when we set our 2011-14 and 2012-15 Strategies were anticipated to be:

Central Case	June 2011	Sept 2011	Dec 2011	Mar 2012	June 2012	Sept 2012	Dec 2012	Mar 2013	June 2013	Sept 2013	Dec 2013	Mar 2014	Jun 2014	Sep 2014
Strategy 2011-14	0.50	0.75	1.00	1.25	1.50	2.00	2.50	2.75						
Strategy 2012-15				0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50

- These interest rate projections are used as the basis for compiling our investment income budget. Clearly interest rates are projected to stay low for a more sustained period and this will be reflected in the investment income we receive. In order to mitigate the risk that interest rates would remain low over 2011/12 we spread the maturity dates for our investments based on our advisor's maturity limit advice. This strategy was undertaken to take advantage of better yields, whilst not compromising the security of our investments. The outcome of this was there was no significant impact on our investment income compared to the budget.

2.2 Investment Strategies Approved Covering the 2011/12 Financial Year

- Council approved two Investment Strategies during 2011/12 and these are shown in **APPENDIX A**.
- In addition, as part of the half year report to Cabinet on 29th November 2011 we amended our investment criteria following the Moody's and Fitch downgrades in October 2011.
- The changes to our Investment Strategy demonstrated how we monitored and updated it on an ongoing basis, seeking Full Council approval for any significant changes to ensure the safe return of our investments.

2.3 Investments and Cash flow

- The investments that the Council had outstanding together with a summary of investment activity throughout the 2011/12 financial year and the maturity profile of our investments compared to interest rate projections are shown at **APPENDIX B**.
- The summary of our investment activity shows that our current list of institutions is short and this reflects the suitability of counter parties available for the Council to invest its monies with. This is a reflection of the credit crunch and the ongoing challenges in the banking sector.
- Our actual average cash flow in 2011/12 was within **8%** of our projected budget (**APPENDIX B)**.
- We received **£165K** in net investment income in 2011/12, compared with a revised Budget of **£154K**, an additional **£11K** of investment income generated.

2.4 The Performance of the Treasury Management Function

- The performance of the Treasury Management function needs to be measured against our investment objectives of Security (the safe return of our monies), Liquidity (making sure we have sufficient money to pay for our services) and Yield (the return on our investments) and these are shown in detail at **APPENDIX C**.
- Our aim for the risk status of our investments was originally **A+**. However, following the Moody's and Fitch downgrades in October 2011 and the reduction in our minimum long term rating criteria, the risk status was revised to **A-**. Our investments at the 31st March 2012 had a more secure risk status of **A+** based on their time length and **AA-** based on their value**.**
- We achieved an average yield of **1.05%** and this compares to our performance indicator of the average 7-day London Inter-bank Bid (LIBID) rate, which was **0.52%**, the 1 month rate was **0.58%,** the 3 month rate was **0.89%** and the 6 month rate was **1.21%.**

2.5 Balance Sheet

- The actual Balance Sheet and Balance Sheet Summary compared with the projected Balance Sheet as at 31 March 2012 are shown at **APPENDIX D**.
- The reasons for the major variances between actual and projections are also shown at **APPENDIX D**.

2.6 Treasury Position

- Our investments (excluding accounting adjustments and other balances) have increased from **£10.130m** on 31 March 2011 to **£12.375m** on 31 March 2012 and the reasons for this increase are shown in the Balance Sheet commentary (**APPENDIX D**).
- Our Treasury Position as at 31 March 2012 is set out at **APPENDIX D**.

2.7 Prudential indicators 2011/12

- Our actual Prudential Indicators are shown in detail at **APPENDIX E** and are summarised in the financial implications section of this report.

2.8 Specified Investments

- On 22 June 2012 Moody's completed its review of credit ratings and downgraded the ratings of 15 banks and securities firms including Barclays, HSBC, and Royal Bank of Scotland.
- Separately the agency has also downgraded the ratings of Lloyds Bank, Bank of Scotland and National Westminster Bank.
- This downgrade means that Royal Bank of Scotland and National Westminster Bank are not currently eligible for new investments because their short term credit rating falls below our minimum level.
- This downgrade also means that we need to consider how we manage our new investments moving forward. The options we have to manage a reduction in the number of banks and building societies available for new investment is:

  - **Option 1** – To remove the minimum short term credit rating. Our Advisors Arlingclose have indicated "in the case of credit ratings, although a number of ratings are considered (long-term, short-term, support and viability), it is the long term rating that is the ultimate driver of creditworthiness of financial institutions.
  - **Option 2** – To extend our list of approved financial institutions to include those domiciled in Canada and Australia subject to a limit being applied.
  - **Option 3** – a combination of the options detailed above.

- Our primary objective in relation to our investments is their safe return and therefore the recommended changes relate to option 3. The changes required to our Annual Investment Strategy are detailed below:

  Specified Investments – Banks and building Societies (changes to Minimum Credit Criteria)

  - To remove the short term credit rating minimum credit criteria and utilise only the long term rating.

  Specified Investments - Banks and building Societies (inclusion of Canadian and Australian Financial Institutions)

  - To further reduce credit risk it is recommended that we include some non European banks within our list of specified investments. Canadian and Australian banks have relatively high credit ratings and therefore due to their high level of credit worthiness and the diversification this provides to our portfolio it is recommended that we include them in our list of specified investments as long as they meet our minimum long term credit rating.
  - To introduce sovereign limits of **25%** of total investments for Canadian financial institutions and **25%** of total investments for Australian financial institutions.

  Our recommended revised list of Specified Investments is shown at **APPENDIX F**

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 Council can confirm that it has complied with its Prudential Indicators for 2011/12, these were originally approved by Council at its meeting on 23rd February 2011 and were fully revised and approved by Council on 22nd February 2012 as part of the Council's Treasury Management Strategy Statement

In compliance with the requirements of the CIPFA Code of Practice this report provides members with a summary report of the Treasury Management Activity during 2011/12. The Prudential Indicators for the Capital Financing Requirement and Actual External Debt are higher than both the Revised and Final Budgets because additional capital expenditure funded by finance Leases was undertaken during the financial year.

None of the other Prudential Indicators have been breached and a prudent approach has been taking in relation to investment activity with priority being given to security and liquidity over yield.

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

Prudential Indicator	Capital Expenditure	Final Budget 2011/12	Actual 2011/12
1	Capital Expenditure **(£m)**	£5.432m	£4.082m
2	Ratio of Financing Costs to Net Revenue Stream (**%**)	5%	4%
3	Capital Financing Requirement (**£m**) Net External Borrowing does not exceed the Capital Financing Requirement in the current and next 2 years	£1.385m True	£1.403m True
4	Actual External Debt (**£m**). (Borrowing and Finance Leases)	£1.323m	£1.350m
5	Incremental impact of Capital Investment Decisions on Band D Council Tax (**£**)	£0.68	£0.47
6	Authorised Limit (**£m**) (Maximum)	£12.113m	£1.803m
7	Operational Boundary (**£m**) (Maximum)	£2.978m	£1.803m
8	Adoption of CIPFA Code of Practice in Treasury Management	Yes	Yes
9	Net Debt (New Indicator) (£m)	-£8.261m	-£11.566m
	Interest Rate Exposure (**%**)		
10	Upper Limit for Investments Fixed Interest Rate Exposure	-100%	-48%
	Upper Limit for Investments Variable Interest Rate Exposure	-100%	-52%
11	Upper Limit for Borrowings Fixed Interest Rate Exposure	100%	100%
	Upper Limit for Borrowings Variable Rate Interest Exposure	30%	0%
	Maturity Structure of Fixed Rate Borrowing (Upper Limit) (**%**)		
12	Under 12 months	100%	100%
	12 months and within 24 months	20%	0%
	24 months and within 5 years	80%	0%
	5 years and within 10 years	40%	0%
	10 years and within 20 years	60%	0%
	20 years and within 30 years	40%	0%
	30 years and within 40 years	40%	0%
	40 years and within 50 years	40%	0%
	50 years and above	20%	0%
13	Principal sums invested >364 days (**£m**)	£2.100m	£0
14	Credit Risk (New Indicator)	We consider security; liquidity and yield, in that order, when making investment decisions	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) Money Market Funds with an AAA rating. c) Deposits with other Local Authorities. d) Business Reserve, Certificates of Deposit and Term Deposits 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.
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
Treasury Management Strategy Report 2011-14 – Cabinet 1 February 2011.
Half Year Report on Treasury Management Services and Projected Prudential Indicators 2011/12 – Cabinet 29 November 2011
Treasury Management Strategy Report 2012-15 – Cabinet 14 February 2012.
The Prudential Code for Capital Finance in Local Authorities

Investment Strategies Approved Covering the 2011/12 Financial Year.

Full Council approved two Investment Strategies during 2011/12 and these are shown in the tables below:

Specified Investments[1]

Financial Asset Category	Strategy Approved 22 February 2012		Strategy Approved 23 February 2011	
	Minimum Criteria	**Limits**	**Minimum Criteria**	**Limits**
UK Banks and Building Societies	Minimum Short Term Rating Fitch = F1 Moody's = P-1 Standard and Poors = A-1 Minimum Long Term Rating Fitch = A- Moody's = A3 Standard and Poors = A-	**£2 million** and subject to Arlingclose advice	Minimum Short Term Rating Fitch = F1 Moody's = P-1 Standard and Poors = A-1 Minimum Long Term Rating Fitch = A+ Moody's = A1 Standard and Poors = A+	**£2 million** and subject to Arlingclose advice
Deposits with Money Market Funds	Fitch = AAAmmf Moodys = Aaa/MR1+ Standard and Poors = AAAm	**£1.5 million**	Fitch = AAAmmf Moodys = Aaa/MR1+ Standard and Poors = AAAm	**£2 million**
UK Government	Not applicable	No limit	Not applicable	No limit
Local Authorities, Parish Councils etc	Not applicable	No limit	Not applicable	No limit

Group Limit	**£3 million**	**£3 million**
Money Market Funds Limit	**No limit**	**£10 million**
Sovereign Limit	100% UK	100% UK

Non Specified Investments

Financial Asset Category	Strategy Approved 22 February 2012		Strategy Approved 23 February 2011	
	Minimum Criteria	**Limits**	**Minimum Criteria**	**Limits**
The Council's own bank (where credit ratings are not sufficient)	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.		Now a specified investment	
Deposits with a maturity of greater than one year	Minimum Short Term Rating Fitch = F1 Moody's = P-1 Standard and Poors = A-1 Minimum Long Term Rating Fitch = A+ Moody's = A1 Standard and Poors = A+	**£2.1 million**	Minimum Short Term Rating Fitch = F1+ Moody's = P-1 Standard and Poors = A-1+ Minimum Long Term Rating Fitch = AA- Moody's = Aa3 Standard and Poors = AA-	**£2.3 million**
Group Limit	**£3 million**		**£3 million**	
Sovereign Limit	100% UK		100% UK	

[1] Specified Investments are the lowest risk investments being in high security and high liquidity investments made in Sterling, Short term investments made with UK Government and other Local Authorities and short term money market transactions with a "high credit quality".

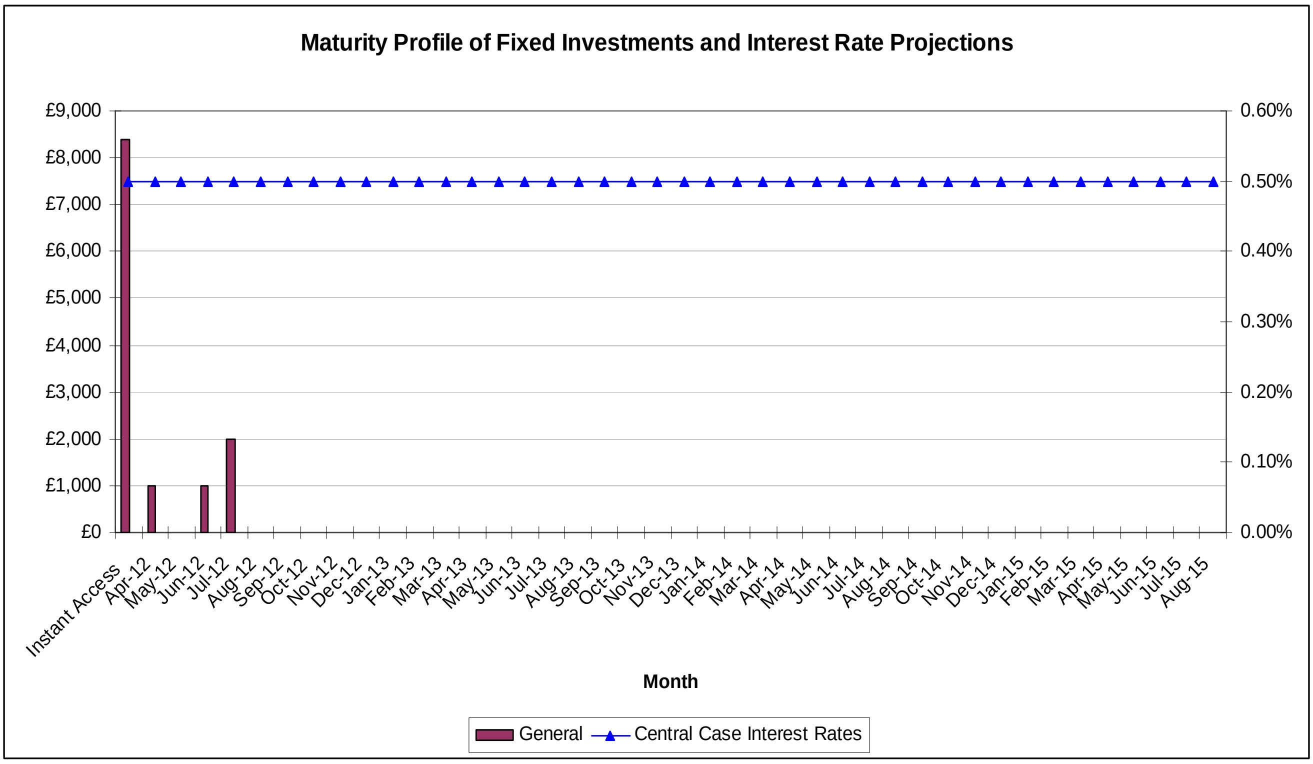
Investments and Cash flow in 2011/12

Investments at 31 March 2012

The table below shows a breakdown of our investments at the end of the financial year:

Counterparty	Principal	Matures	Days to Maturity	Rate	Credit Rating	Foreign Parent
Money Market Funds						
Deutsche Bank	£1,135,000	01-Apr-12	Instant Access	0.73%	AAA	N/A
Ignis	£1,135,000	01-Apr-12	Instant Access	0.77%	AAA	N/A
Prime Rate	£1,135,000	01-Apr-12	Instant Access	0.83%	AAA	N/A
Insight	£470,000	01-Apr-12	Instant Access	0.67%	AAA	N/A
Other Counterparties						
Bank of Scotland	£1,000,000	16-Apr-12	16	2.05%	A	No
LloydsTSB	£2,000,000	18-Jul-12	109	2.05%	A	No
Barclays Bank	£1,000,000	20-Jun-12	81	1.47%	A	No
Santander UK Bank	£2,000,000	01-Apr-12	Instant Access	0.75%	A+	Yes
RBS Bank	£1,000,000	01-Apr-12	Instant Access	0.80%	A	No
NatWest Bank	£1,500,000	01-Apr-12	Instant Access	0.80%	A	No
Total Investments	**£12,375,000**					
Accounting Adjustments and Other Balances	£541,000					
Balance Sheet Total	**£12,916,000**					

The graph below compares the current maturity profile of our investments at the 31st March 2012 to our projections for interest rates. This shows we are continuing to keep the maturity profile of our portfolio relatively short to manage the risks of interest rate increases together with enabling us to be able to react to changes in the credit risk of counterparties.



However, the previous table and graph only shows the investment position on one particular day of the financial year, the table below shows a summary for the whole of the financial year:

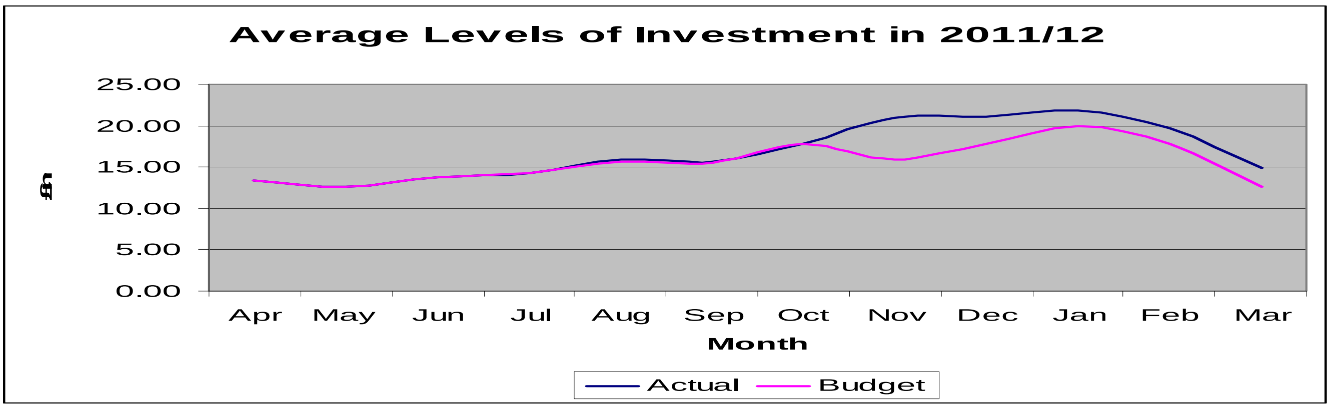
Counterparty	Number of Deals	Total Principal Invested	Is the Counterparty on our list of eligible institutions at 31 March 2012?
Blackrock	35	£18,335,000	Yes
Debt Management Office	5	£15,050,000	Yes
Santander UK	27	£15,000,000	Yes
Deutsche Bank	16	£13,580,000	Yes
Invesco Aim	14	£11,250,000	Yes
Ignis	11	£9,650,000	Yes
JP Morgan	11	£8,755,000	Yes
Legal & General	7	£7,580,000	Yes
SWIP	5	£4,620,000	Yes
NatWest	6	£2,780,000	Yes
Insight	2	£2,400,000	Yes
Prime Rate	1	£2,000,000	Yes
Barclays Bank	2	£2,000,000	Yes
Lloyds TSB	1	£2,000,000	Yes
Nationwide	1	£2,000,000	Yes
Royal Bank of Scotland	3	£1,750,000	Yes
BNY Mellon	1	£1,500,000	Yes
Bank of Scotland	1	£1,000,000	Yes
Fife Council	1	£1,000,000	Yes
Midlothian Council	1	£1,000,000	Yes
Yorkshire Bank	1	£300,000	No
Total	**152**	**£123,550,000**	

This list is reviewed on an ongoing basis and takes account of the following sources of information:

- Advice from our Treasury Management advisors.
- Credit Ratings.
- Credit Default Swaps prices.
- Share Prices.
- Information in the general and financial media.

Cash flow for 2011/12

The graph below compares the budget for average investment levels in 2011/12 with the actual levels.



The graph shows that the actual trend of investments followed the budgeted trend quite closely.

Investment Income and Borrowing Cost Performance for 2011/12

Net Investment Income

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.

The interest rates, amounts of money we had available to invest, interest receipts, interest paid and net investment income is shown in the table below:

Details	**2011/12 Original**	**2011/12 Final Budget**	**2011/12 Actual**
Average Amount we had available to Invest (£m)	£12.44m	£15.59m	£16.87m
Average Interest Rate (%)	1.16%	1.05%	1.05%
Interest Receipts	£133,000	£167,000	£179,551
Interest Paid	(£13,000)	(£12,500)	(£14,514)
Net Investment Income (£)	**£120,000**	**£154,500**	**£165,037**

External Borrowing Costs

No new borrowing was undertaken in 2011/12.

Performance of the Treasury Management Function

The performance of the Treasury Management function should be measured against the investment objectives of Security (the safe return of our monies), Liquidity (making sure we have sufficient money to pay for our services) and Yield (the return on our investments).

Security

Our aim for the risk status of our portfolio was **A-** utilising the lowest rating from the three credit rating agencies**.**

The investments outstanding at the 31 March 2012 had a risk status of **A+** based on the length of the investment and **AA-** based on the value of the investment, which is a more secure risk status. These risk statuses are both compliant with our aim and the recommendations from our Treasury Management advisors.

In addition, we are currently keeping the length of our investments relatively short term to ensure that we can react to changes in counterparty credit risk very easily. At the 31 March 2012 our Treasury Management advisors had recommended new investments were for the following periods:

Bank or Building Society	Investment Time Limit
Santander (UK)	Overnight
Lloyds	1 month
Bank of Scotland	1 month
Barclays	1 month
HSBC	3 months
Royal Bank of Scotland	1 month
National Westminster Bank	1 month
Nationwide Building Society	1 month
Standard Chartered	3 months

The time limits were relatively short to manage counterparty credit risk (a bank or building society being unable to repay our investment). We also maintained balances in Money Market Funds and Instant Access Accounts to provide for unforeseen cash flow requirements.

The average length of investments we made in 2011/12 was **80 days**.

Liquidity

Measuring the performance in relation to liquidity is a much more difficult task and the easiest way to assess performance is to see how frequently we needed to borrow on a temporary basis during the financial year. We are actively managing liquidity risk in 2012/13 by purchasing Certificates of Deposit and Treasury Bills because they can be sold on the secondary market in the event the money is required for unforeseen circumstances. We also have significant sums invested in call accounts and Money Market Funds which provide instant access to cash.

Therefore, due to the level of our liquid investments in 2011/12 we did not need to temporarily borrow.

Yield

In 2011/12 we achieved an average interest rate of **1.05%** and this compares to our performance indicator of the average 7-day London Inter-bank Bid (LIBID) rate, which was **0.52%**, the 1 month rate was **0.58%,** the 3 month rate was **0.89%** and the 6 month rate was **1.21%.**

Balance Sheet

Property, Plant and Equipment and the Revaluation Reserve restated by **£0.455m** for the inclusion of Heritage Assets from 1 April 2010.	31 Mar 2011 Actual £m	31 Mar 2012 Actual £m	31 Mar 2012 Final Budget £m	Variance To Final Budget £m
1. Property, Plant and Equipment, Investment Property & Intangible Assets	51.104	47.892	48.832	-0.940
4. Long Term Debtors	0.236	0.248	0.215	-0.033
Current Assets				
4. Current Assets (including accrued interest)	5.797	3.289	5.797	-2.508
2. Short Term Investments (excluding accrued interest)	7.448	4.059	9.583	3.331
2. Cash and Cash Equivalents	2.846	8.857		
Current Liabilities				
3. Short Term Borrowing	-0.005	-0.004	-0.005	0.001
3. Finance Leases	-0.523	-0.503	-0.568	0.065
4. Short Term Creditors	-7.046	-6.753	-7.046	0.293
4. Provisions	0	-0.039	0	-0.039
4. Receipts in Advance	-0.247	-0.061	-0.089	0.028
Long Term Liabilities				
3. Finance Leases	-1.240	-0.810	-0.720	-0.090
3. Borrowing	-0.035	-0.033	-0.030	-0.003
4. Pension Scheme	-20.187	-25.037	-20.187	-4.850
4. Receipts in Advance	-0.863	-0.554	-0.279	-0.275
Total Assets less Liabilities	**37.285**	**30.551**	**35.503**	**-4.952**

Usable Reserves				
4. Capital Grants Unapplied	-1.636	-1.269	-0.882	-0.387
5. Usable Capital Receipts	-2.087	-1.443	-1.677	0.234
5. Burntwood Leisure Centre Sinking Fund	-0.665	-0.538	-0.456	-0.082
5. Burntwood Synthetic Pitch Sinking Fund	-0.029	-0.029	-0.029	0
5. City Centre Redevelopment Sinking Fund	-0.024	-0.025	-0.024	-0.001
5. King Edwards Leisure Centre Sinking Fund	-0.031	-0.031	-0.031	0
5. Lombard Street Car Park Sinking Fund	-0.017	-0.034	-0.017	-0.017
5. Elections	-0.095	-0.075	-0.095	0.020
5. Public Open Spaces	-0.007	-0.006	-0.007	0.001
5. Three Spires Multi Storey Reserve	-0.994	-1.124	-1.141	0.017
5. Earmarked Reserves	-1.419	-1.697	-1.359	-0.338
5. Grant Aid	-0.038	-0.046	-0.038	-0.008
5. General Fund Balance	-3.406	-3.076	-2.728	-0.348
Unusable Reserves				
1. Revaluation Reserve	-5.387	-4.939	-4.932	-0.007
1. Capital Adjustment Account	-41.873	-41.550	-42.512	0.962
4. Deferred Credits	-0.011	-0.010	-0.009	-0.001
4. Benefits Payable during Employment	0.233	0.296	0.233	0.063
5. Collection fund	0.014	0.008	0.014	-0.006
4. Pension Scheme	20.187	25.037	20.187	4.850
Total Equity	**37.285**	**30.551**	**35.503**	**4.952**

Balance Sheet Summary

1. Capital Financing Requirement	3.844	1.403	1.388	0.015
2. Investments (including Accounting Adjustments and Other Balances)	10.294	12.916	9.583	3.331
3. Borrowing and Finance Leases	-1.803	-1.350	-1.323	-0.027
4. Net Creditors	-3.537	-4.853	-2.060	-2.793
5. Balances and Reserves	-8.798	-8.116	-7.588	-0.528

Balance Sheet Commentary

The main changes to the budget and its assumptions that impacted on the Balance Sheet are detailed below:

Pensions

The triennial valuation of the pension fund took place in 2011/12 using new assumptions such as CPI etc and this valuation has resulted in the Pension scheme liability increasing from **£20.187m** to **£25.037m**.

Debtors

The level of debtors has reduced from a budgeted level of **£5.797m** to an actual level of **£3.289m** because a collection fund (Government) debtor has now become a creditor (ie we budgeted that they would owe the Council money and the Council actually owes them money) and the level of manual sundry debtors has reduced.

Treasury Portfolio

The Balance Sheet can be used to assess the underlying need to borrow (known as the Capital Financing Requirement). The table below shows that we had sufficient balances and reserves to mean we did not need to undertake any long-term borrowing in 2011/12.

31 Mar 2011 Actual £m	Details	31 Mar 2012 Original £m	31 Mar 2012 Revised £m	31 Mar 2012 Final £m	31 Mar 2012 Actual £m
3.844	The amount of our capital spend that is not financed from capital receipts, revenue, grants and contributions (Capital Financing Requirement)	1.037	1.324	1.385	1.403
-1.803	Less: current funding provided through finance leases and long term borrowing	-1.036	-1.323	-1.323	-1.350
2.041	**Borrowing Need**	**0.001**	**0.001**	**0.062**	**0.053**
-10.448	Less: the level of our balances and reserves we currently hold as investments	-6.602	-7.609	-7.588	-8.116
-£8.407m	**Our net borrowing need (a positive figure indicates when we need to borrow)**	**-£6.601m**	**-£7.608m**	**-£7.526m**	**-£8.063m**

Our current Balance Sheet projections indicate we could continue to follow this strategy for the medium term. However, we will need to constantly review these projections in line with changes to our budgets.

APPENDIX E

COMPLIANCE WITH PRUDENTIAL INDICATORS 2011/12

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. It should be noted that CIPFA undertook a review of the Code in early 2008 and issued revised Code in November 2009.

The Council implemented its strategy within the limits and parameters set in its treasury policy, strategy statement and Prudential Indicators against the prevailing market conditions and opportunities as follows:

(a) Financing its capital spending from government grants / usable capital resources / revenue contributions, etc. rather than from external borrowing.

(b) Adhering to the paramount requirement of safeguarding the council's invested balances during a period of unprecedented money market dislocation; maintaining adequate diversification between institutions; optimising investment returns subject to the overriding requirement of security and liquidity.

(d) Forecasting and managing cash flow and undertaking short-term borrowing and lending to preserve the necessary degree of liquidity.

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, nor are there any difficulties envisaged for future years.

3. Estimates of Capital Expenditure (Prudential Indicator 1):

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.

Capital Financing	**2011/12 Original £m**	**2011/12 Revised £m**	**2011/12 Final £m**	**2011/12 Actual £m**
Non Current Assets	1.885	2.944	3.124	2.647
Revenue Expenditure Funded from Capital under Statute	1.498	2.497	2.308	1.435
Total	**£3.383m**	**£5.441m**	**£5.432m**	**£4.082m**

3.2 This capital expenditure has been financed as follows:

Capital Financing	**2011/12 Original £m**	**2011/12 Revised £m**	**2011/12 Final £m**	**2011/12 Actual £m**
Capital receipts	0.996	1.687	1.710	0.858
Burntwood Sinking Fund	0.112	0.209	0.210	0.126
Capital Grants and Contributions	2.161	3.392	3.256	4.848
Revenue contributions and earmarked reserves	0.060	0.099	0.075	0.149
Unfinanced Expenditure	0	0	0.082	0.053
Finance Leases	0.054	0.054	0.099	0.099
Total	**£3.383m**	**£5.441m**	**£5.432m**	**£6.133m**

4. Ratio of Financing Costs to Net Revenue Stream (Prudential Indicator 2):

4.1 This is an indicator of affordability and demonstrates the revenue implications of capital investment decisions by highlighting the proportion of the revenue budget required to meet the borrowing costs associated with capital spending. The financing costs include existing and proposed capital commitments.

4.2 The ratio is based on costs net of investment income.

Ratio of Financing Costs to Net Revenue Stream	2011/12 Original %	2011/12 Revised %	2011/12 Final %	2011/12 Actual %
General Fund	0	5	5	4
Total	**0%**	**5%**	**5%**	**4%**

5. Capital Financing Requirement (Prudential Indicator 3):

5.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. In order to ensure that over the medium term net borrowing will only be for a capital purpose, the Council ensures that net external borrowing does not, except in the short term, exceed the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years.

Capital Financing Requirement	2011/12 Original £m	2011/12 Revised £m	2011/12 Final £m	2011/12 Actual £m
General Fund	1.037	1.324	1.385	1.403
Total	**£1.037m**	**£1.324m**	**£1.385m**	**£1.403m**

6. Actual External Debt (Prudential Indicator 4):

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 31/03/2012	Short Term £m	Long Term £m	Total £m
	Borrowing	0.004	0.033	0.037
	Finance Leases	0.503	0.810	1.313
	Total	**£0.507m**	**£0.843m**	**£1.350m**

7. Incremental Impact of Capital Investment Decisions (Prudential Indicator 5):

7.1 This is an indicator of affordability that shows the impact of Capital investment decisions on Council Tax levels when the budget for the year was set.

Incremental Impact of Capital Investment Decisions	2011/12 Original £	2011/12 Revised £	2011/12 Final £	2011/12 Actual £
Incremental Impact of Capital Investment Decisions	0	0.14	0.68	0.47
Total	**£0**	**£0.14**	**£0.68**	**£0.47**

8. Affordable Borrowing Limit, 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 CFR.

8.2 The **Authorised Limit (Prudential Indicator 6):** This is the maximum amount of external debt that can be outstanding at one time during the financial year. The limit, which is expressed gross of investments, is consistent with the Council's existing commitments, proposals for capital expenditure and financing and with its approved treasury policy and strategy and also provides headroom over and above for unusual cash movements. This limit was set at **£12.113m** for 2011/12.

8.3 **Operational Boundary (Prudential Indicator 7)**: This is limit is set to reflect the Council's best view of the most likely prudent (i.e. not worst case) levels of borrowing activity and was originally set at **£2.981m** and revised to **£2.978m** for the financial year.

8.4 Levels of debt are measured on an ongoing basis during the year for compliance with the Authorised Limit and the Operational Boundary. The Council maintained its total external borrowing and other long-term liabilities within both limits; at its peak this figure was:

Details	**£000s**
External Borrowing	40
Bank Overdraft	0
Other Long Term Liabilities (Finance Leases) (Maximum Outstanding)	1,763
Total	**1,803**

9. Adoption of the CIPFA Treasury Management Code (Prudential Indicator 8):

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 CIPFA Treasury Management Code within its treasury policies, practices and procedures. At its meeting on 23rd February 2011 the Council originally approved its Prudential Indicators for 2011/12. The Prudential Indicators were fully revised and approved by Council on 22nd February 2012.

10. Gross and Net Debt (Prudential Indicator 9)

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

Gross and Net Debt	**2011/12 Original £m**	**2011/12 Revised £m**	**2011/12 Final £m**	**2011/12 Actual £m**
Outstanding Borrowing (at nominal value)	New Indicator	0.035	0.035	0.037
Other Long-term Liabilities (at nominal value)		1.288	1.288	1.313
Gross Debt		**1.323**	**1.323**	**1.350**
Less : Investments		-10.981	-9.584	-12.916
Net Debt		**-9.658**	**-8.261**	**-11.566**

11. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure (Prudential Indicators 10 and 11):

11.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The exposures are calculated on a gross basis. The upper limit for variable rate exposure allows for the use of variable rate debt to offset exposure to changes in short-term rates on our portfolio of investments.

No.	Interest Rate Exposures	2011/12 Original %	2011/12 Revised %	2011/12 Final %	2011/12 Actual (during the financial year) %		
					Highest	**Lowest**	**Average**
	Fixed Interest Rates						
10	Upper Limit for Fixed Interest Rate Exposure	-100	-100	-100	-80	-23	-48
	Upper Limit for Fixed Interest Rate Exposure	100	100	100	100	100	100
	Net Fixed Exposure	**0%**	**0%**	**0%**	**-20%**	**-77%**	**-52%**
	Variable Interest Rates						
11	Upper Limit for Variable Rate Exposure	-75	-100	-100	-77	-20	-52
	Upper Limit for Variable Interest Rate Exposure	30	30	30	0	0	0
	Net Variable Exposure	**-45%**	**-70%**	**-70%**	**-77%**	**-20%**	**-52%**

12. Maturity Structure of Fixed Rate borrowing (Prudential indicator 12):

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	Lower Limit %	Upper Limit %	Actual Borrowing as at 31/3/2012 £	Percentage of total as at 31/3/2012 %
	Under 12 months	0	100	37,000	100%
	12 months and within 24 months	0	20	0	0
	24 months and within 5 years	0	80	0	0
	5 years and within 10 years	0	40	0	0
	10 years and within 20 years	0	60	0	0
	20 years and within 30 years	0	40	0	0
	30 years and within 40 years	0	40	0	0
	40 years and within 50 years	0	40	0	0
	50 years and above	0	20	0	0

12.3 The only long-term fixed rate borrowing the Council currently has is in relation to a brewery loan of **£0.037m**.

13. Upper Limit for total principal sums invested over 364 days (Prudential Indicator 13):

13.1 This indicator is set in order to allow the Council to manage the risk inherent in investments longer than 364 days. For 2011-12 this limit was originally set at **£2.10m**. At their peak, these investments totalled **£0m**.

14. Credit Risk (Prudential Indicator 14):

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.

Use of 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 long-term ratings assigned by various agencies which may include Moody's Investors Services, Standard & Poor's, Fitch Ratings.

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

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%**. This means up to **100%** of investments can be placed with UK Domiciled banks and building societies.
- The Sovereign Limits for Canadian financial institutions will be **25%** of total investments and for Australian financial institutions will be **25%** of total investments.

APPENDIX F

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
Term Deposits / Certificates of Deposit / Call Accounts	Australia	Australia and New Zealand Banking Group	New Counterparty	£2m
Term Deposits / Certificates of Deposit / Call Accounts	Australia	Commonwealth Bank of Australia	New Counterparty	£2m
Term Deposits / Certificates of Deposit / Call Accounts	Australia	National Australia Bank Ltd (National Australia Bank Group)	New Counterparty	£2m
Term Deposits / Certificates of Deposit / Call Accounts	Australia	Westpac Banking Corp	New Counterparty	£2m
Term Deposits / Certificates of Deposit / Call Accounts	Canada	Bank of Montreal	New Counterparty	£2m
Term Deposits / Certificates of Deposit / Call Accounts	Canada	Bank of Nova Scotia	New Counterparty	£2m
Term Deposits / Certificates of Deposit / Call Accounts	Canada	Canadian Imperial Bank of Commerce	New Counterparty	£2m
Term Deposits / Certificates of Deposit / Call Accounts	Canada	Royal Bank of Canada	New Counterparty	£2m
Term Deposits / Certificates of Deposit / Call Accounts	Canada	Toronto-Dominion Bank	New Counterparty	£2m

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 arrangement