



Haringey Council
Agenda item:

General Purposes Committee

On 12 January 2010

Report Title.	Treasury Management Strategy Statement (TMSS) and Investment Strategy 2010/11 to 2012/13; and Treasury Management 3rd Quarter Performance update for the period ended 31 December 2009	
Report of:	Chief Financial Officer	
Signed :	 Gerald Almeroth	
Contact Officer :	Kevin Bartle, Head of Corporate Finance Telephone 020 8489 3743	
Wards(s) affected: All	Report for: Non Key Decision	
1. Purpose of the report		
1.1.	To present the Treasury Management Strategy Statement 2010/11 to 2012/13 to be adopted by the Cabinet and the Council.	
1.2.	To update the committee on the Council's treasury management activities for the third quarter and period ended 31 December 2009.	
2. Recommendations		
2.1	That the Treasury Management Strategy Statement and Investment Strategy 2010/11 to 2012/13 is agreed and recommended to the Cabinet and Council for approval.	
2.2	That Members endorse in principle the changes to the Council's Constitution described in section 8 of the report and request the Constitution Review Working Group to recommend them, once set out in more detail, to the full Council for	

adoption.

- 2.2 That Members note the Treasury Management activity undertaken for the third quarter and period ended 31 December 2009.

3. Reason for recommendation(s)

- 3.1. To agree a Treasury Management Strategy Statement for 2010/11 to 2012/13 for approval by Cabinet and Council and to seek members endorsement in principle of the proposed changes to the Council's constitution.
- 3.2. To ensure members are aware of the Treasury Management activities undertaken in the third quarter of 2009/10 and to report on performance.

4. Summary

- 4.1. This report sets out the Council's Treasury Management Strategy Statement for 2010/11 to 2012/13 and provides a performance review for the third quarter and period ended 31 December 2009.

5. Head of Legal Services Comments

- 5.1 The Head of Legal Services has been consulted on the content of this report and comments that the recommendations are within the policy agreed by Council and consistent with the purposes of Financial Regulations. In considering the recommendations Members must take into account the expert financial advice available in the report and any further advice given at the meeting of the Committee in relation to the level of risk inherent in the proposals. Certain of the matters described in section 8 of the report will require changes to the Council's Constitution, principally in the Financial Regulations, and these changes will be the subject of a more detailed report to the Constitution Review Working Group and a resulting report to full Council.

6. Use of appendices

- Appendix A (shown as Appendix K to the Financial Planning Report to Cabinet on 26 January 2010) – Treasury Management Strategy Statement and Investment Strategy 2010/11 to 2012/13;
- Appendix B – Investments Performance Indicator.

7. Local Government (Access to Information) Act 1985

The following background papers were used in the preparation of this report:

- Financial Planning Report for 2009/10 to 2011/12 reported to Council and agreed on 23 February 2009.
- Reports to General Purposes Committee dated 7 July 2009 and 22 October 2009.

For access to the background papers or any further information please contact Kevin Bartle, Head of Corporate Finance, on 0208 489 3743.

8. Treasury Management Strategy Statement and Investment Strategy 2010/11 to 2011/12/13

- 8.1 The Council is required to consider an annual Treasury Management Strategy (TMSS) under the CIPFA Code of Practice on Treasury Management, which was adopted by the Council in May 2002. CIPFA has recently issued a revised Code of Practice in response to the turmoil in financial markets which was caused by the 'Credit Crunch'. The Council's revised TMSS attached as Appendix A to this report contains a number of amendments principally concerning scrutiny and reporting requirements. The revised TMSS is recommended to the Cabinet and Council for approval.

The Revised CIPFA Code of Practice on Treasury Management 2009

- 8.2 There are a number of changes within the new Code which are concerned principally with the status of the Code within Public Service organisations and reporting and scrutiny requirements as follows:

Standing Orders

- 8.3 CIPFA recommends that local authorities adopt, as part of their standing orders/ financial regulations, the following four clauses:

- 8.3.1 This organisation (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 (TMP), 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 content of the policy statement and TMP will follow the recommendation contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of this Council. Such amendments will not result in the organisation materially deviating from the Code's key principles.
- 8.3.2 The Council will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMP.
- 8.3.3 The Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to the General Purposes Committee, and for the execution and administration of treasury management decisions to the Chief Financial Officer, who will act in accordance with the organisation's policy statement and TMP and, if he/she is a CIPFA member, CIPFA's *Standard of Professional Practice on Treasury Management*.

- 8.3.4 The Council nominates the Audit Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.
- 8.4 The effect of adopting the above clauses will lead to the following changes to the current reporting arrangements.
- 8.4.1 **The Council** in addition to agreeing the TMSS and receiving an annual report following closure of the accounts, it is now a requirement of the Code that a mid year review of Treasury Management operations be submitted for consideration.
- 8.4.2 **The General Purposes Committee** will continue to receive quarterly reports on the implementation and regular monitoring of the treasury management policies and practices. In addition, it will now formulate the TMSS prior to its scrutiny by the Audit Committee and subsequent adoption by the Council.
- 8.4.3 **The Audit Committee** will assume responsibility for ensuring effective scrutiny of the TMSS prior to its consideration by the Council.
- 8.5 The Local Government Act 2003 also requires the Council to have regard to the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.
- 8.6 The Local Government Act 2003 and the CIPFA Prudential Code introduced a new prudential system for local authority capital finance and came into effect on 1 April 2004. The key objectives of the code are to ensure:
- capital investment plans are affordable, prudent and sustainable;
 - treasury management decisions are taken in accordance with good professional practice; and,
 - fulfilment of the above objectives by setting out prudential indicators that must be set and monitored.
- 8.7 In line with the suggestion in the ODPM investment guidance, the Treasury Management Strategy Statement and Annual Investment Strategy have been combined into one document. This is set out in full in Appendix A and includes the proposed prudential indicators for 20010/11 to 2012/13.
- 8.8 The strategy is based upon the Council's Treasury officers' views on interest rates, supplemented with leading market forecasts provided by the Council's external treasury advisor, Arlingclose. The strategy covers:
- background information on the treasury management operation;
 - the balance sheet and treasury position;
 - the outlook for interest rates;
 - borrowing requirement and strategy;
 - investment policy and strategy;

- balanced budget requirements;
- the 2010/11 minimum revenue provision (MRP) statement;
- reporting, and,
- other items.

Investment Policy and Strategy

- 8.9 The annual investment policy forms part of the TMSS set out in the appendix. There are some changes proposed and to be considered which reflect the signs of improvement seen in the financial sector post the 'credit crunch'.
- 8.10 At present, investments in banks and building societies (on a term, at call or on a certificate of deposit basis) are limited to UK banks and building societies that have a minimum AA- long-term credit rating and F1+ short-term rating and are participants in the UK Government's Credit Guarantee Scheme. This currently limits activity to seven UK institutions all of which have maximum investment limits of £20m at group level and term durations of a maximum of 12 months.
- 8.11 Following an improvement in market conditions in the financial sector, the Council's treasury advisors, Arlingclose, are presently recommending that in order to diversify the counterparty list, the use of comparable non-UK banks should now be considered for investment.
- 8.12 The sovereign states whose banks are recommended for inclusion are Australia, Canada, Finland, France, Germany, Netherlands, Spain, Switzerland and the US. The banks selected by Arlingclose have been considered after analysis and careful monitoring of:
- Credit Ratings (minimum long-term AA-)
 - Credit Default Swaps
 - GDP, net debt as a percentage of GDP
 - Sovereign Support Mechanism/potential support from a well resourced parent institution; and,
 - Share price.
- 8.13 Arlingclose has taken into account information on corporate developments and market sentiment towards the counterparties. However, given that these recommendations have only very recently been provided to the Council, officers have not had the opportunity to undertake due diligence into these institutions and consequently are unable to recommend that any of these proposed institutions be added to the counterparty list at present.
- 8.14 It is anticipated that in-house due diligence will be completed by April 2010, and that subject to a satisfactory outcome to this process, some or all of the potential counterparties be added, potentially on the following cautionary bases:-

- Minimum credit rating AA Long-term F1+ Short Term. This compares to the existing UK Institutions where the Council currently requires a long-term credit rating of a minimum of AA-.
- Maximum exposure to any one institution (or group) of £10m. This compares with the existing UK counterparty limit of £20m per institution (or group).

8.15 At present, the Council has approved investment limits of up to £10m in Money Market Funds with a maximum exposure limit to any one fund of £5m. In accordance with his delegated authority, the Chief Financial Officer, in consultation and with the agreement of the General Purposes Committee, has recently appointed three firms of Money Market Fund managers. These funds have proved particularly useful in the management of the treasury operation in terms of security (short-term high quality paper and deposits), liquidity (immediate recall of cash), thereby reducing external borrowing on a number of occasions, and yield (typically 20 basis points higher than placements with the DMO). It is recommended, therefore, that the maximum total investment in Money Market Funds be increased from £10m to £45m subject to a maximum exposure to any one fund of £15m.

Icelandic Investments

8.16 The administration process for the Icelandic banks in which Council deposits are held is continuing. It is now reported that two interim payments have been received in respect of Heritable Bank amounting to £5,726,195.44 (equivalent to circa 29p in the pound of the deposits with that bank). The position with investments in respect of those held in Glitnir Bank has changed in that the Glitnir Winding Up Board recently decided not to allow priority status to local authorities' deposit claims. A formal objection to this decision has been filed. Further information will be provided to General Purposes Committee and Cabinet once the position is clearer. The position in relation to Landsbanki Bank remains unchanged.

8.17 The government has issued a regulation to allow authorities to defer accounting for the net loss until 2010/11. The latest estimate of the impairment to be charged to the Council's accounts assumes an estimated recovery of 80.6% of the total capital sum invested in all Council Icelandic investments. This amounts to £7.1m and will need to be written off in 2010/11. This can be funded from the capital redemption reserve of £10m. The Council has, however, accounted for interest not received in relation to these investments in 2008/09.

8.18 The DCLG has recently advised that Authorities can request permission to capitalise the losses that may result from the Icelandic investments. Haringey Council has applied for permission to capitalise the costs which would mean that the loss could be financed over a period of up to 20 years from 2009/10.

9. Performance Update – 3rd Quarter and Period ended 31 December 2009

9.1 In accordance with the recommendations contained in the Treasury Management Strategy Statement (TMSS) and approved by the Council on 23 February 2009, there is a requirement to report to members the Treasury Management activity on a half yearly basis. However, reports are now made to GP Committee on a quarterly basis on all significant matters affecting the operation of the TMSS. This third report outlines the Council's treasury management activities for the period ended December 2009.

10. Treasury Management Activities for the Quarter Ended 31 December 2009

10.1 In October 2008, the Chief Financial Officer undertook a risk assessment into the institutions holding council deposits, the results of which prompted a move to revise the Council's approved counterparty list.

10.2 The revised counterparty list was included in the 2009/10 TMSS, was ratified by full Council in February 2009 and incorporates the following:

'The Council will only invest (on a term or certificate basis) in UK banks and building societies that have a minimum AA- long term and F1+ short term credit rating AND are participants in the UK Government's Credit Guarantee Scheme (CGS).'

10.3 This formalised the action already taken to limit the Council's investment activity to the following banks:-

- Abbey National;
- Barclays;
- HSBC;
- Lloyds Banking Group;
- Royal Bank of Scotland; and the following Building Society;
- Nationwide.

In addition investments in the above institutions are restricted to a maximum limit of £20m per institution with a maximum duration of 12 months. Furthermore, investment activity, and thus the counterparty limit, is also limited to the Group concerned. The Council, could not, for example invest £20m in each of Lloyds Bank and the Bank of Scotland given their group relationship.

10.4 The effect of adopting this lending list is set out in Table 1 below which compares the investment portfolio reported by the Chief Financial Officer in October 2008 to the current portfolio profile at 29 December 2009 as follows:

Table 1

Institution	Value Oct 2008 £m	Maturity dates	Value 29 Dec 2009 £m	Maturity dates
UK Banks	1.5	Oct 08	64.9	Dec 09 – Apr 10
UK Building Societies	58.7	Oct 08 – Aug 09	10.0	Nov 09
Irish Banks	61.1	Oct 08 – Jun 09	0	n/a
Irish Building Societies	12.0	Oct 08 – Feb 09	0	n/a
Other Non – UK Banks	23.4	Oct 08 – Nov 09	0	n/a
Money Market Funds	0		10.0	30 Dec 09
Debt Management Office	0		6.3	30 Dec 09
TOTAL	156.7		91.2	

Note: This table includes Pension Fund but excludes Icelandic investments.

- 10.5 It can be seen from the table, the significant impact that the revisions to the TMSS has had. This includes eliminating the exposure to Irish building societies and banks and other non-UK banks. In addition, investments in UK building societies have been reduced by £48.7m to £10m. These reductions have been matched by compensating increases in the exposure to UK banks, money market funds and the government's Debt Management Office (DMO). The DMO is an investment facility operated by the UK government which has the highest security rating but conversely pays a very low interest rate in comparison to other institutions. A list of all outstanding deposits is set out at Appendix B.
- 10.6 The security of investments remains the principal investment objective for this authority. Appendix B sets out a performance indicator, which has been developed in conjunction with the treasury management advisors, and provides a credit rating based objective scoring analysis.
- 10.7 The credit risk scores of 3.5 (value weighted average) and 4.0 (time weighted average) indicate a low level of security risk based on the methodology adopted by our treasury advisors as set out at the foot of the table as follows:

Above target (AAA to AA+, Score 0-2)

Target score (AA to A+, Score 3-5)

Below target (below A+, Score over 5)

Credit risk scores 2009/2010

	1 st quarter as at 30 Jun 09	2 nd quarter as at 30 Sep 09	3 rd quarter as at 31 Dec 09
Value Weighted	4.3	3.5	3.5
Time Weighted	4.3	4.0	4.0

- 10.8 On this basis, Haringey is within the target range. The scores achieved in this quarter are similar to those reported in quarter 2 but show an improvement over those reported in quarter 1 of 4.3 and 4.3 respectively.
- 10.9 Although the Council has adopted a more prudent stance in respect of the treasury management function it has still been possible to out perform the investment performance indicator over the eight months (ended November) of 2009/10 as follows:

Target: 0.5% above Base Rate
Actual Investment performance: 0.6338% above Base Rate

Interest Rate Outlook

- 10.10 The TMSS is predicated on interest rate forecasts provided by the Council's Treasury Management advisors, currently Arlingclose. The latest forecast compared to the version used in the estimates is shown as Annex 3 to Appendix A (Appendix K to the Cabinet Financial Planning report). It can be seen that the base rate is now forecast to remain constant at 0.5% until September 2010 but could rise by a series of phased increases to 4% by December 2011. The interest rate outlook is important because it affects borrowing decisions and the term of future investments and hence the capacity to maximise interest earned. The Council would not, for example, want to invest for periods in excess 12 months given that the rates are likely to increase in the medium term.

Interest Earned in the period ended 30 September 2009

- 10.11 The interest earnings in the third quarter are forecast to amount to £0.135m, making £1.275m for the year to date. The budget for investment income in 2009/10 is £2 million. Based on a forecast of earnings for the fourth quarter to 31 March 2010 it is likely that the total investment income for 2009/10 will amount to approximately £1.35m. The shortfall of £0.65m (compared to the estimate of £2m) is due to the pattern of investment replacement, i.e. new deposits are being made at lower rates than those maturing and capital expenditure which is currently being financed by revenue balances pending long-term borrowing.

11. Recommendations

- 11.1 That the Treasury Management Strategy Statement and Investment Strategy 2010/11 to 2012/13 is agreed and recommended to the Cabinet and Council for approval.
- 11.2 That Members endorse in principle the changes to the Council's Constitution described in section 8 of the report and request the Constitution Review Working Group to recommend them, once set out in detail, to the full Council for adoption.
- 11.3 That Members note the Treasury Management activity undertaken for the third quarter and period ended 31 December 2009.

**Treasury Management Strategy Statement
and Investment Strategy 2010/11 to 2012/13**

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1. Background
2. Balance Sheet and Treasury Position
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Annexes

1. Current and Projected Portfolio Position
2. Prudential Indicators
3. Interest Rate Outlook
4. Specified and non-specified Investments for use by the Council

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drivers of Treasury Management Activity. The estimates, based on the current Revenue budget and Capital Programmes, are set out below:

	31 Mar 10 Estimate £000	31 Mar 11 Estimate £000	31 Mar 12 Estimate £000	31 Mar 13 Estimate £000
CFR	677,587	718,766	777,471	822,697
Balances & Reserves	18,025	15,687	16,076	16,076
Net Balance Sheet Position	659,562	703,079	761,395	806,621

- 2.2. The Council's level of physical debt and investments is linked to these components of the Balance Sheet. The current portfolio position is set out at Annex 1. Market conditions, interest rate expectations and credit risk considerations will influence the Council's strategy in determining the borrowing and investment activity against the underlying Balance Sheet position.
- 2.3. As the CFR represents the level of borrowing for capital purposes and revenue expenditure cannot be financed from borrowing, net physical external borrowing should not exceed the CFR other than for short term cash flow requirements. It is permissible under the Prudential Code to borrow in advance of need up to the level of the estimated CFR over the term of the Prudential Indicators. Where this takes place the cash will form part of its invested sums until the related capital expenditure is incurred. This being the case net borrowing should not exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years other than in the short term due to cash flow requirements.
- 2.4. The move to International Financial Reporting Standards (IFRS) has implications for the Capital Financing Requirement components on the Balance Sheet. Analysis of the Council's Private Finance Initiative (PFI) schemes and Operating leases against IFRS requirements may result in the related long term assets and liabilities being brought onto the Council's Balance Sheet. The estimates for the CFR and Long Term Liabilities will therefore need to take into account such items. This will influence the determination of the Council's Affordable Borrowing Limit and Operational Boundary.
- 2.5. The Department for Communities and Local Government has recently consulted on proposals to reform the council housing subsidy system. The proposed Self-financing option would require a one-off reallocation of housing debt. As the consultation period has only recently ended and the mechanism for debt transfer has not been determined, the estimates set out in this strategy do not take into account any potential debt transfer that may arise in future years.

3. Outlook for Interest Rates

The economic interest rate outlook provided by the Council's treasury advisor, Arlingclose Ltd, is attached at Annex 3. Financial markets remain reasonably volatile as the structural changes necessary within economies and the banking system evolve. This volatility provides opportunities for active treasury management. The Council will reappraise its strategy from time to time and, if

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- 4.5. The Council's strategy is to maintain maximum control over its borrowing activities as well as flexibility on its loans portfolio. Capital expenditure levels, market conditions and interest rate levels will be monitored during the year in order to minimise borrowing costs over the medium to longer term. A prudent and pragmatic approach to borrowing will be maintained to minimise borrowing costs without compromising the longer-term stability of the portfolio, consistent with the Council's Prudential Indicators.
- 4.6. In conjunction with advice from its treasury advisor, Arlingclose Ltd, the Council will keep under review the options it has in borrowing from the PWLB, the market and other sources identified in the Treasury Management Practices Schedules – up to the available capacity within its CFR and Affordable Borrowing Limit (defined by CIPFA as the Authorised Limit).

The outlook for borrowing rates:

- 4.7. Short-dated gilt yields are forecast to be lower than medium and long-dated gilt yields during the financial year. Despite additional gilt issuance to fund the UK government's support to the banking industry, short-dated gilts are expected to benefit from expectations of lower interest rates as the economy struggles through a recession. Yields for these maturities will fall as expectations for lower interest rates mount.
- 4.8. The differential between investment earnings and debt costs, despite long term borrowing rates being around historically low levels, remains acute and this is expected to remain a feature during 2010/11. The so-called 'cost of carry' associated with long term borrowing compared to temporary investment returns means that the appetite for new long term borrowing brings with it additional short-term costs. It is not surprising that the use of internal resources in lieu of borrowing has been the most cost effective means of financing capital expenditure but, at some stage, internal resources will become depleted and require topping up.
- 4.9. PWLB variable rates have fallen below 1%. They are expected to remain low as the Bank Rate is maintained at historically low levels to enable the struggling economy emerge from the recession. Against a backdrop of interest rates remaining lower for longer and a continuation of the 'cost of carry' backdrop, then a passive borrowing strategy i.e. borrow long term funds as they are required, may remain appropriate. Equally, variable rate funds (that avoid the cost of carry) or EIP (equal instalments of principal) that mitigate the impact are both active considerations.
- 4.10. Decisions to borrow at low, variable rates of interest will be taken after considering the absolute level of longer term interest rate equivalents and the extent of variable rate earnings on the Council's investment balances. When longer term rates move below the cost of variable rate borrowing any strategic exposure to variable interest rates will be reviewed and, if appropriate, reduced.
- 4.11. The PWLB remains the preferred source of borrowing given the transparency and control that its facilities continue to provide.

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- security of the invested capital;
- liquidity of the invested capital;
- an optimum yield which is commensurate with security and liquidity.
- The CLG's recent (draft) revised Guidance on investments, reiterates security and liquidity as the primary objectives of a prudent investment policy.

The speculative procedure of borrowing purely in order to invest is unlawful.

- 6.3. Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the CLG Guidance. Potential instruments for the Council's use within its investment strategy are contained in Annex 4.
- 6.4. The credit crisis has refocused attention on the treasury management priority of security of capital monies invested. The Council will continue to maintain a counterparty list based on its 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 including monitoring of credit default swaps, share price movements and press comment.
- 6.5. The Council's current level of investments is presented at Annex 1.

Investment Strategy

- 6.6. The global financial market storm in 2008 and 2009 has forced investors of public money to reappraise the question of risk versus yield. Income from investments is a key support in the Council's budget.
- 6.7. The UK Bank Rate has been maintained at 0.5% since March 2009. Short-term money market rates are likely to remain at very low levels which will have a significant impact on investment income. The Council's strategy must however be geared towards this development whilst adhering to the principal objective of security of invested monies.
- 6.8. The Chief Financial Officer under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Decisions taken on the core investment portfolio will be reported to the General Purposes Committee on a quarterly basis.

Investments managed in-house:

- 6.9. The Council's shorter term cash flow investments are made with reference to the outlook for the UK Bank Rate and money market rates.
- 6.10. In any period of significant stress in the markets, the default position is for investments to be made with the Debt Management Agency Deposit Facility.
- 6.11. 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)

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recently appointed three firms of Money Market Fund managers. These funds have proved particularly useful in the management of the treasury operation in terms of security (short-term high quality paper and deposits), liquidity (immediate recall of cash), thereby reducing external borrowing on a number of occasions, and yield (typically 20 basis points higher than placements with the DMO). **The maximum total investment in Money Market Funds is increased from £10m to £45m subject to a maximum exposure to any one fund of £15m. Annex 4 reflects this change.**

- 6.18. To protect against a prolonged period of low interest rates, 1-year deposits and longer-term secure investments will be actively considered within the limits the Council has set for Non-Specified Investments (see Annex 4). The longer-term investments will be likely to include:
- **Supranational bonds (bonds issued by multilateral development banks):** The joint and individual pan-European government guarantees in place on these bonds provide security of the principal invested. Even at the lower yields likely to be in force, the return on these bonds will provide certainty of income against an outlook of low official interest rates.
 - **UK government guaranteed bonds and debt instruments issued by banks/building societies:** The UK Government's 2008 Credit Guarantee Scheme permits specific UK institutions to issue short-dated bonds with an explicit government guarantee. The bonds are issued at a margin over the underlying gilt and would be a secure longer-term investment option.

Investments which constitute capital expenditure

- 6.19. Investments meeting the definition of capital expenditure can be financed from capital or revenue resources. They are also subject to the CLG's Guidance on "non-specified investments". Placing of such investments has accounting, financing and budgetary implications. Whilst it is permissible to fund capital investments by increasing the underlying need to borrow, it should be noted that under the CLG's MRP Guidance, MRP must be applied over a 20 year period.
- 6.20. The Council has determined a maximum of £60m limit to investments which constitute capital expenditure.
- 6.21. All investment activity will comply with the accounting requirements of the local authority SORP.

7. Balanced Budget Requirement

- 7.1. The Council complies with the provisions of Section 32 of the Local Government Finance Act 1992 to set a balanced budget.

8. 2010/11 MRP Statement

- 8.1. For many years local authorities have been required by Statute and associated Statutory Instruments to charge to the Revenue Account an annual provision for the repayment of debt associated with expenditure incurred on capital assets. This charge to the Revenue Account was referred to as the Minimum Revenue Provision (MRP).

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each year, or

(b) Annuity: where the principal repayments increase over the life of the asset

- 8.9. MRP commences in the financial year following that in which the expenditure is incurred or, in the year following that in which the relevant asset becomes operational. This enables an MRP “holiday” to be taken in relation to assets which take more than one year to be completed before they become operational.
- 8.10. The estimated life of the asset will be determined in the year that MRP commences and will not be subsequently revised. However, additional repayments can be made in any year which will reduce the level of payments in subsequent years.
- 8.11. If no life can be reasonably attributed to an asset, such as freehold land, the life is taken to be a maximum of 50 years. In the case of freehold land on which a building or other structure is constructed, the life of the land will be treated as equal to that of the structure, where this would exceed 50 years.
- 8.12. In instances where central government permits revenue expenditure to be capitalised, the Statutory Guidance sets out the number of years over which the charge to revenue must be made.

Option 4 - Depreciation Method

- 8.13. The depreciation method is similar to that under Option 3 but MRP is equal to the depreciation provision required in accordance with proper accounting practices to be charged to the Income and Expenditure account.

Conditions of Use

- 8.14. The CLG Guidance puts the following conditions on the use of the four options:

Options 1 and 2 can be used on all capital expenditure incurred before 1 April 2008 and on Supported Capital Expenditure on or after that date.

Options 3 and 4 are considered prudent options for Unsupported Capital Expenditure on or after 1 April 2008. These options can also be used for Supported Capital Expenditure whenever incurred.

Policy

- 8.15. The policy will be to use **Option 1** (Regulatory Method) for supported borrowing and **Option 3** (Asset Life Method) for unsupported borrowing.

9. Reporting on the Treasury Outturn

The Chief Financial Officer will report on treasury management activity/performance as follows:

- (a) Quarterly to the General Purposes Committee against the strategy approved for the year.
- (b) The Council will receive a mid-year report and an outturn report on its treasury

**Treasury Management Strategy Statement
and Investment Strategy 2010/11 to 2012/13**

ANNEX 1

EXISTING PORTFOLIO PROJECTED FORWARD

	Portfolio at 31 March 09 £000	31 Mar 10 Estimate £000
External Borrowing:		
Fixed Rate – PWLB	508,611	543,902
Fixed Rate – Market	125,000	125,000
Variable Rate – PWLB	-	-
Variable Rate – Market	-	-
Other long-term liabilities	42,984	38,403
Total External Debt	676,595	707,305
Investments:		
<i>Managed in-house</i> Deposits and monies on call	109,457	65,000
Total Investments	109,457	65,000
Net Borrowing position	567,138	642,305

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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 is set out at paragraph 87 of the Prudential Code.

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

No. 3	Ratio of Financing Costs to Net Revenue Stream	2009/10 Approved %	2009/10 Revised %	2010/11 Estimate %	2011/12 Estimate %	2012/13 Estimate %
	Non-HRA	5.20	5.35	4.67	4.35	4.37
	HRA	33.59	32.77	33.39	32.47	30.85

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 CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and its financing. It is an aggregation of the amounts shown for Fixed and Intangible assets, the Revaluation Reserve, the Capital Adjustment Account, Government Grants Deferred and any other balances treated as capital expenditure.

No. 3	Capital Financing Requirement	2009/10 Approved £000	2009/10 Revised £000	2010/11 Estimate £000	2011/12 Estimate £000	2012/13 Estimate £000
	Non-HRA	226,850	228,256	229,702	238,874	242,600
	HRA	449,242	449,331	489,064	538,597	580,186
	Total CFR	676,092	677,587	718,766	777,471	822,786

5.2 The year-on-year change in the CFR is due to the following

Capital Financing Requirement	2009/10 Revised £000	2010/11 Estimate £000	2011/12 Estimate £000	2012/13 Estimate £000
Balance B/F	642,926	677,587	718,766	777,471
Capital expenditure financed from borrowing (per 3.2)	43,898	50,309	67,893	54,870
Revenue provision for debt Redemption.	(9,237)	(9,130)	(9,188)	(9,555)
Other items				
Balance C/F	677,587	718,766	777,471	822,786

6. Actual External Debt:

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.

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

No.7	Operational Boundary for External Debt	2009/10 Approved £000	2009/10 Revised £000	2010/11 Estimate £000	2011/12 Estimate £000	2012/13 Estimate £000
	Borrowing	870,419	870,870	871,046	871,232	871,428
	Other Long-term Liabilities	4,581	4,130	3,954	3,768	3,572
	Total	875,000	875,000	875,000	875,000	875,000

9. Adoption of the CIPFA Treasury Management Code:

9.1 This indicator demonstrates that the Council has adopted and will continue to adopt the principles of best practice.

No. 8	Adoption of the CIPFA Code of Practice in Treasury Management
	The Council approved and will adopt the new CIPFA Treasury Management Code 2009 at its meeting in February 2010.

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

10.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. This Council calculates these limits on a net interest paid basis (i.e. interest paid on fixed rate debt net of interest received on fixed rate investments)

10.2 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. The limit allows for the use of variable rate debt to offset exposure to changes in short-term rates on investments

		2009/10 Approved %	2009/10 Revised %	2010/11 Estimate %	2011/12 Estimate %	2012/13 Estimate %
No. 9	Upper Limit for Fixed Interest Rate Exposure	100	100	100	100	100
No. 10	Upper Limit for Variable Interest Rate Exposure	40	40	40	40	40

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

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ANNEX 3

Arlingclose's Economic and Interest Rate Forecast

	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12
Official Bank Rate										
Upside risk				+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	0.50	0.50	0.50	0.50	1.00	1.50	2.25	3.00	4.00	4.00
Downside risk					-0.50	-0.50	-0.50	-0.25	-0.25	-0.25
1-yr LIBID										
Upside risk				+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	1.25	1.25	1.25	1.50	2.00	2.75	3.50	4.00	4.25	4.25
Downside risk					-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
5-yr gilt										
Upside risk		+0.25	+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	2.60	2.70	2.80	2.90	3.00	3.25	3.50	3.75	4.00	4.25
Downside risk		-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
10-yr gilt										
Upside risk			+0.25	+0.25	+0.25	+0.25	+0.25	+0.25	+0.25	+0.25
Central case	3.60	3.75	3.75	4.00	4.00	4.25	4.25	4.50	4.50	4.75
Downside risk			-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
20-yr gilt										
Upside risk		+0.25	+0.25	+0.25	+0.25	+0.25	+0.25	+0.25	+0.25	+0.25
Central case	4.10	4.25	4.50	4.75	4.75	5.00	5.00	5.00	5.00	5.00
Downside risk		-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
50-yr gilt										
Upside risk	+0.25	+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	4.00	4.25	4.50	4.50	4.50	4.75	4.75	4.75	4.75	4.75
Downside risk			-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25

- The recession has taken a toll on global economies which are past the worst but still vulnerable. The recovery in growth is likely to be hesitant and uneven, more "W" than "V" shaped.
- The pace and sustainability of UK recovery is still very uncertain; policy rates will remain low for some while. Gilt yields are increasingly volatile and will remain so.
- The Federal Reserve will keep policy rates on hold for an extended period. The ECB will only hike rates after a durable upturn in growth.

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ANNEX 4

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 DMO’s Debt Management Account Deposit Facility
- Deposits with UK local authorities
- Deposits with banks and building societies
- Certificates of deposit with banks and building societies
- *Gilts : (bonds issued by the UK government)
- Bonds issued by multilateral development banks
- AAA-rated Money Market Funds with a Constant Net Asset Value (Constant NAV)
- Other Money Market Funds and Collective Investment Schemes– i.e. credit rated funds which meet the definition of a collective investment scheme as defined in SI 2004 No 534 and SI 2007 No 573.

For credit rated counterparties, the minimum criteria will be the short-term / long-term ratings assigned by:

Long Term Minimum	AA-
Short term	FI+

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

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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:

	In-house use	Maximum maturity	Capital expenditure?	Maximum Counterparty Limit
Gilts and bonds <ul style="list-style-type: none"> ▪ Gilts ▪ Bonds issued by multilateral development banks ▪ Bonds issued by financial institutions guaranteed by the UK government, e.g. GEFCO ▪ Sterling denominated bonds by non-UK sovereign governments 	✓ (on advice from treasury advisor)	<u>6 years</u>	No	£60m
Government guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies (e.g. govt bonds issued by HBOS / RBS / Nationwide, etc)	✓	<u>6 years</u>	Yes	£60m

Note: 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.

29/12/2009

INSTITUTION:	Group	Principal	Matures	Days to maturity	Rate	Credit rating (source Bloomberg)	Credit Risk Score
(a) Outstanding deposits							
Abbey Time Deposits	Santander	£5,125,000.00	04/01/2010	6	0.54%	AA-	4
Abbey -call account	Santander	£770,000.00	30/12/2009	1	0.80%	AA-	4
Abbey -call account	Santander	£525,000.00	30/12/2009	1	0.80%	AA-	4
Abbey -call account	Santander	£13,500,000.00	30/12/2009	1	0.80%	AA-	4
Lloyds	Lloyds Banking Group	£5,000,000.00	06/04/2010	98	1.32%	AA-	4
Lloyds	Lloyds Banking Group	£5,000,000.00	30/04/2010	122	1.33%	AA-	4
Lloyds	Lloyds Banking Group	£5,000,000.00	08/01/2010	10	1.65%	AA-	4
Lloyds	Lloyds Banking Group	£5,000,000.00	27/01/2010	29	0.50%	AA-	4
Nationwide Building Society		£6,750,000.00	04/01/2010	6	0.41%	AA-	4
Nationwide Building Society		£3,200,000.00	18/01/2010	20	0.41%	AA-	4
Goldman Sachs Money Market Fund		£5,000,000.00	30/12/2009	1	0.50%	AAA	1
Hendersons Money Market Fund		£5,000,000.00	30/12/2009	1	0.50%	AAA	1
RBS	RBS	£5,000,000.00	03/03/2010	64	0.98%	AA-	4
Barclays	Barclays	£5,500,000.00	18/01/2010	20	0.53%	AA-	4
Barclays	Barclays	£4,500,000.00	29/01/2010	31	1.09%	AA-	4
Barclays	Barclays	£10,000,000.00	15/01/2010	17	1.25%	AA-	4
DMO		£6,349,000.00	30/12/2009	1	0.25%	AAA	1
Total		£ 91,219,000		22/01/2010	0.817%		
Number of deposits							
Value Weighted Average		£ 5,365,824				AA	3.5
Time Weighted Average				24		AA-	4.0

Credit risk scored 1 - 10 : 1 = strongest rating lowest risk, i.e. AAA, through to 15 = lowest credit rating, highest risk, i.e. D
Non-rated, non-guaranteed institutions score 11

Above target (AAA to AA+ Score 0-2)

Target (AA to AA+ Score 3-5)

Below target (Anything less than A+ Score above 5)

On this basis, Haringey is in the middle of the target range