Haringey Council
Agenda item:

Audit Committee On 01 February 2010

Report Title.	**Treasury Management Strategy Statement (TMSS) and Investment Strategy 2010/11 to 2012/13**
Report of: Signed :	**Chief Financial Officer** **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 for scrutiny prior to its adoption by the Cabinet and the Council and following its agreement by the General Purposes Committee.

2. Recommendations

2.1 That the Treasury Management Strategy Statement and Investment Strategy 2010/11 to 2012/13 is scrutinised and comments made prior to its approval by the Council.

2.2 That Members note the changes to the Council's Constitution described in section 8 of the report.

3. Reason for recommendation(s)

3.1. To scrutinise the Treasury Management Strategy Statement for 2010/11 to 2012/13 for approval by Cabinet and Council.

4. Summary

4.1. This report sets out the Council's Treasury Management Strategy Statement for 2010/11 to 2012/13.

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.

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.

- TMSS report to the General Purpose Committee on 12 January 2010.

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 20112/13

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 to this report, contains a number of amendments principally concerning the investment policy, scrutiny of the TMSS and reporting requirements. The revised TMSS is recommended to the 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 Cabinet and 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.

8.9 As stated in paragraph 8.1, the recommended amendments to the TMSS, principally concern the investment policy, scrutiny of the TMSS and reporting requirements. Revisions to the Investment Policy and Strategy are highlighted in some detail for members' attention in the paragraphs below. In relation to other areas of the TMSS, the majority of policies and strategies remain as in previous years; the list below sets out matters for the particular attention of members: -

- The underlying need to borrow for capital purposes as measured by the Capital Financing Requirement (CFR) together with Balances and Reserves are the core drivers of Treasury Management activity. The CFR has been proposed in line with the planned Capital Programme to be approved by Cabinet and Council in February 2010;

- There are no proposed changes to the Council's Authorised Limit and Operational Boundary for External Debt;

- The Council has £125m of loans which are LOBO loans (Lender's Options Borrower's Option) of which £50m of loans are currently in or will be in their option state in 2010-11. In the event that the lender exercises the option to change the rate or terms of the loan, the Council will consider the terms being provided and also repayment of the loan without penalty. It is now proposed that the default position will be to repay the loans;

- The Minimum Revenue Provision (MRP) policy is not currently proposed for change however the Council will wish to review the policy in consultation with its Treasury Management Advisors in light of the Council's medium term financial position. Any proposal to change policy will require the approval of Council.

Investment Policy and Strategy

8.10 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'.

8.11 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.

8.12 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.

8.13 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.

8.14 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.

8.15 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).

8.16 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. Further explanation of Money Market Funds and their benefits are set out in the next paragraph.

Money Market Funds

8.17 Money Market Funds (MMFs) are pooled funds that invest in short-term debt instruments. They provide the benefits of pooled investments, as investors can participate in a more diverse and high-quality portfolio than they otherwise could individually.

8.18 Each investor who invests in a money market fund is considered a shareholder of the investment pool, a part owner of the fund.

8.19 The principal objectives of MMFs are the preservation of capital, very high liquidity and competitive returns commensurate with security and liquidity. The most important characteristic of a MMF is the highly diversified, high credit quality investments in the fund.

8.20 The recommendation to extend our exposure to MMFs is based on the lower risk associated with a diverse and high quality portfolio coupled with the liquidity afforded by such instant access instruments.

Icelandic Investments

8.21 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.

8.22 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.

8.23 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. Recommendations

9.1 That the Treasury Management Strategy Statement and Investment Strategy 2010/11 to 2012/13 is scrutinised and comments made prior to its approval by the Council.

9.2 That Members note the changes to the Council's Constitution described in section 8 of the report.

Appendix K

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

Contents

Annexes

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

1. Background

1.1. The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") requires local authorities to determine the Treasury Management Strategy Statement (TMSS). This statement also incorporates the Investment Strategy. Together, these cover the financing and investment strategy for the forthcoming financial year.

In response to the financial crisis in 2008 and the collapse of the Icelandic banks, CIPFA has recently revised the TM Code and Guidance Notes as well as the Prudential Indicators. The Department for Communities and Local Government (CLG) is currently in the process of revising and updating the Investment Guidance.

1.2. 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."

1.3. 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 is 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 & Regulatory Risk

1.4. 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 (Annex 1), the Prudential Indicators (Annex 2) and the outlook for interest rates (Annex 3).

1.5. The purpose of this Treasury Management Strategy Statement is to approve:

- Treasury Management Strategy for 2010-11 (Borrowing - Section 4, Debt Rescheduling - Section 5, Investments - Section 6)
- Prudential Indicators – Annex 2 (NB - PI No. 6 - The Authorised Limit is a statutory limit)
- MRP Statement – Section 8
- Use of Specified and Non-Specified Investments – Annex 4

2. Balance Sheet and Treasury Position

2.1. The underlying need to borrow for capital purposes as measured by the Capital Financing Requirement (CFR) together with Balances and Reserves are the core drivers of Treasury Management Activity. The estimates, based on the current Revenue budget and Capital Programmes, are set out below:

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

	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	822,786
Balances & Reserves	18,025	15,687	16,076	16,076
Net Balance Sheet Position	659,562	703,079	761,395	806,710

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. The CFR represents the level of borrowing for capital purposes. Consequently, 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. <u>Outlook for Interest Rates</u>

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 needs be, realign it with evolving market conditions and expectations for future interest rates.

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

4. Borrowing Requirement and Strategy

4.1. The Council's underlying need to borrow for capital purposes is measured by reference to its Capital Financing Requirement (CFR) – see Annex 2. The CFR represents the cumulative capital expenditure of the local authority that has not been financed. To ensure that this expenditure will ultimately be financed, local authorities are required to make a Minimum Revenue Provision for Debt Redemption (MRP) from within the Revenue budget each year.

4.2. Capital expenditure not financed from internal resources (i.e. Capital Receipts, Capital Grants and Contributions, Revenue or Reserves) will produce an increase in the CFR (the underlying need to borrow) and in turn produce an increased requirement to charge MRP in the Revenue Account.

4.3. Physical external borrowing may be greater or less than the CFR, but in accordance with the Prudential Code, the Council will ensure 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.

4.4. The cumulative estimate of the maximum long-term borrowing requirement is estimated by comparing the projected CFR with the profile of the current portfolio of external debt and long term liabilities over the same financial horizon, as follows:

	31/03/2010 Estimate £000	**31/03/2011 Estimate £000**	**31/03/2012 Estimate £000**	**31/03/2013 Estimate £000**
Capital Financing Requirement	677,587	718,766	777,471	822,786
Less: Existing Profile of Borrowing and Other Long Term Liabilities	642,926	677,587	718,766	777,471
Cumulative Maximum External Borrowing Requirement	34,661	41,179	58,705	45,315
Balances & Reserves	18,025	15,687	16,076	16,076
Cumulative Net Borrowing Requirement/Investments	16,636	25,492	42,629	29,239

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.

4.12. The Council has £125m loans which are LOBO loans (Lender's Options Borrower's Option) of which £50m of loans are currently in or will be in their option state in 2010-11. In the event that the lender exercises the option to change the rate or terms of the loan, the Council will consider the terms being provided and also repayment of the loan without penalty. The default position will be to repay the loans. The Council may utilise cash resources for repayment or may consider replacing the loan(s) by borrowing from the PWLB.

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

5. Debt Rescheduling

5.1. The Council will maintain a flexible policy for debt rescheduling. Market volatility and the steep yield curve may provide opportunities for rescheduling debt from time to time. The rationale for rescheduling would be one or more of the following:

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

5.2. In September 2009, the PWLB issued a Consultation document, entitled 'PWLB Fixed Rates', where the PWLB is reviewing the frequency of rate setting (currently daily) and could move to a live pricing basis. The deadline for the consultation period is 08/01/2010. The likely outcome of this is a reduction in the extent of the margins between premature repayment and new borrowing rates, particularly for longer maturities.

5.3. Any rescheduling activity will be undertaken within the Council's treasury management policy and strategy. The Council will agree in advance with Arlingclose the strategy and framework within which debt will be repaid/rescheduled if opportunities arise. Thereafter the Council's debt portfolio will be monitored against equivalent interest rates and available refinancing options on a regular basis. As opportunities arise, they will be identified by Arlingclose and discussed with the Council's officers.

5.4. All rescheduling activity will comply with the accounting requirements of the local authority SORP and regulatory requirements of the Capital Finance and Accounting Regulations (SI 2007 No 573 as amended by SI 2008/414).

5.5. Borrowing and debt rescheduling activity will be reported to the next meeting of the General Purposes Committee.

6. Investment Policy and Strategy

Background

6.1. Guidance from CLG on Local Government Investments in England requires that an Annual Investment Strategy (AIS) be set.

Investment Policy

6.2. To comply with the CLG's guidance, the Council's general policy objective is to invest its surplus funds prudently. The Council's investment priorities are:

- security of the invested capital;
- liquidity of the invested capital;
- an optimum yield which is commensurate with security and liquidity.
- The 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. However, the yield curve is relatively steep and opportunities will be taken to exploit this situation. Although cognisant of this development, the Council's strategy will continue to adhere to it's 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)
- Deposits with other local authorities
- Business reserve accounts and term deposits
- Bonds issued by Multilateral Development Banks

Annex 4 contains a breakdown of the current counterparties, instruments, instruments and limits in operation.

6.12. 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. These institutions are set out in Annex 4.

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

6.13. 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.

6.14. 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-);
- Share price (of the institution);
- Credit Default Swaps;
- GDP, net debt as a percentage of GDP;
- Sovereign Support Mechanism/potential support from a well resourced parent institution.

6.15. 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.

6.16. 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 (or equivalent). 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).

6.17. 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). 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).

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

8.3. The CLG Guidance recommends that before the start of the financial year, a statement of MRP policy for the forthcoming financial year is approved by the full Council.

8.4. The broad aim of the Policy is to ensure that MRP is charged over a period that is reasonably commensurate with the period over which the capital expenditure which gave rise to the debt provides benefits. In the case of borrowing supported by Revenue Support Grant, the aim is that MRP is charged over a period reasonably commensurate with the period implicit in the determination of that grant. MRP is not required to be charged to the

Housing Revenue Account. Where a local authority's overall CFR is £nil or a negative amount there is no requirement to charge MRP.

MRP Options:

8.5. Four options for prudent MRP provision are set out in the CLG Guidance. Details of each are set out below with a summary set out in Table 1:

Option 1 – Regulatory Method:

8.6. This method replicates the position that would have existed under the previous Regulatory environment. MRP is charged at 4% of the Authority's underlying need to borrow for capital purposes; the Capital Financing Requirement (CFR). The formula includes an item known as "Adjustment A" which was intended to achieve neutrality between the CFR and the former Credit Ceiling which was used to calculate MRP prior to the introduction of the Prudential System on 1 April 2004. The formula also took into account any reductions possible related to commutation of capital related debt undertaken by central government.

Option 2 – CFR Method:

8.7. This method simplifies the calculation of MRP by basing the charge solely on the authority's CFR but excludes the technical adjustments included in Option 1. The annual MRP charge is set at 4% of the non-housing CFR at the end of the preceding financial year.

Option 3 – Asset Life Method:

8.8. Under this method MRP is determined by the life of the asset for which the borrowing is undertaken. This can be calculated by either of the following methods:

(a) Equal Instalments: where the principal repayment made is the same in 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.

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

Option 4 - Depreciation Method

8.13. The deprecation 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. <u>Reporting on the Treasury Outturn</u>

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 activity no later than 30th September after the financial year end.
(c) The audit committee will be responsible for the scrutiny of treasury management activity and practices.

10. <u>Other items</u>

Member Training

10.1. CIPFA's revised Code requires the Chief Financial Officer to ensure that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities.

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

ANNEX 1

EXISTING PORTFOLIO PROJECTED FORWARD

	Balances at 31 March 09 £000	Estimates at 31 March 10 £000	Estimates at 31 March 11 £000
External Borrowing:			
Fixed Rate – PWLB	520,572	564,470	614,779
Fixed Rate – Market	130,475	130,475	130,475
Variable Rate – PWLB	-	-	-
Variable Rate – Market	-	-	-
Other long-term liabilities	42,984	41,310	39,545
Total External Debt	694,031	736,255	784,799
Investments:			
Managed in-house			
Deposits and monies on call	99,731	65,000	65,000
Total Investments	99,731	65,000	65,000
Net Borrowing position	594,300	671,255	719,799

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

ANNEX 2

PRUDENTIAL INDICATORS 2010/11 TO 2012/13

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. The outcome from that review has now been published and there are no material changes to the 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 Chief Financial Officer reports that the authority had no difficulty meeting this requirement in 2009/10, nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3. **Estimates of Capital Expenditure:**

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 and in the case of the HRA, housing rent levels.

No. 1	Capital Expenditure	2009/10 Approved £000	2009/10 Revised £000	2010/11 Estimate £000	2011/12 Estimate £000	2012/13 Estimate £000
	Non-HRA	149,280	121,981	95,956	60,590	46,537
	HRA*	49,725	60,479	52,642	63,142	54,498
	Total	**199,005**	**182,460**	**148,598**	**123,732**	**101,035**

3.2 Capital expenditure will be financed as follows:

Capital Financing	2009/10 Approved £000	2009/10 Revised £000	2010/11 Estimate £000	2011/12 Estimate £000	2012/13 Estimate £000
Capital receipts	9,837	7,752	5,520	14,423	15,477
Government Grants	111,038	88,465	67,160	23,730	10,250
Other Grants etc	7,785	17,986	4,943	4,377	7,329
Major Repairs Allowance	12,407	18,966	12,909	12,909	12,909
Revenue contributions	12,330	5,393	7,757	400	200
Supported borrowing	42,186	39,771	40,497	59,893	54,870
Unsupported borrowing	3,422	4,127	9,812	8,000	0
Total	**199,005**	**182,460**	**148,598**	**123, 732**	**101,035**

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

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.

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

No.4	Actual External Debt as at 31/03/2009	£m
	Borrowing	651.0
	Other Long-term Liabilities	43.0
	Total	**694.0**

7. Impact of Capital Investment Decisions:

7.1 This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and Housing Rent levels. The 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. The full council tax and housing rent figures are shown below for information.

No.5	Impact of Capital Investment Decisions	2009/10 Approved £	2010/11 Estimate £	2011/12 Estimate £	2012/13 Estimate £
	Band D Council Tax	1,184.32	1,184.32	1,219.85	1,256.44
	Average Weekly Housing Rents	82.05	83.20	87.36	91.72

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 CFR.

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	2009/10 Approved £000	2009/10 Revised £000	2010/11 Estimate £000	2011/12 Estimate £000	2012/13 Estimate £000
	Borrowing	895,419	858,690	860,455	862,317	864,279
	Other Long-term Liabilities	4,581	41,310	39,545	37,683	35,721
	Total CFR	**900,000**	**900,000**	**900,000**	**900,000**	**900,000**

8.5 The **Operational Boundary** links directly to the Council's estimates of the CFR 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 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	833,690	835,455	837,317	839,279
	Other Long-term Liabilities	4,581	41,310	39,545	37,683	35,721
	Total CFR	**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.

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

11. Maturity Structure of Fixed Rate borrowing:

11.1 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.

11.2 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.11	Maturity structure of fixed rate borrowing	Lower Limit %	Upper Limit %
	under 12 months	0	25
	12 months and within 24 months	0	25
	24 months and within 5 years	0	50
	5 years and within 10 years	0	100
	10 years and above	0	100

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

12.1 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.

		2009/10 Approved £m	2009/10 Revised £m	2010/11 Estimate £m	2011/12 Estimate £m	2012/13 Estimate £m
No.12	Upper Limit for total principal sums invested over 364 days	60	60	60	60	60

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

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.

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

<u>Underlying assumptions :</u>

- The global financial system is fragile and although sentiment has improved, economies have yet to show consistent signs of recovery.
- UK **growth** contracted 5.2% in the year to September. There is no evidence of the economy exiting from recession – despite forecasts to the contrary – which is supported by weak real economic data and rising unemployment.
- **Looming bank regulation** and capital requirements will curb banking lending activity and is likely to be offset by a reduction in the Reserve Rate.
- **Recovery could be slow and protracted**, affected by the continuing adjustments in household, bank and public sector balance sheets.
- **Official interest rates remain at 0.5%. Quantitative Easing (QE)** could be expanded to beyond £200bn to address the sluggish economy.
- **Inflation** is falling, albeit slowly. CPI could dip below 1% in 2009 and be below the MPC's 2% target over the 2-year forecast horizon. RPI has been negative since March. Weakened sterling remains a risk, but is likely to be overshadowed by a slow recovery.
- The growing budgetary imbalances and bloated central bank balance sheets need credible and sustainable action. **UK gilt supply** is at record levels; the rising ratio of debt to GDP remains unaddressed. **Cuts in public spending and tax increases** are unpalatable but are necessary and inevitable. The risk of failed gilt auctions remains high although **QE is, for now, providing an effective balance to the supply side dynamic**.
- Buoyed by leading indicators and sentiment, equity markets are overoptimistically pricing in a quick, V-shaped recovery, but earnings growth may not be sustained over subsequent quarters.
- The likely political make-up of the next Parliament will increasingly have a bearing on the financial markets. Already the political agenda has rapidly shifted from the avoidance of cuts to their inevitability.

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	F1+

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

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

Specified investments will be made within the following limits:

Instrument	Country	Counterparty	Maximum Limit of Investments in Group (where applicable) £m	Fitch Credit Rating as at 31 December 2009		Maximum Term of Investment
				Long Term	Short Term	
Term Deposits	UK	DMO's Debt Management Account Deposit Facility	No limit	AAA	F1+	6 months
Term Deposits	UK	Other UK Local Authorities	£30m (per Local Authority)	N/A	N/A	364 days
Term Deposits/ Call Accounts	UK	Santander UK Plc (formerly known as Abbey)	£20m	AA-	F1+	364 days/Instant access
Term Deposits/ Call Accounts	UK	Lloyds TSB Bank Plc (Lloyds Banking Group)	£20m	AA-	F1+	364 days/Instant access
Term Deposits/ Call Accounts	UK	Bank of Scotland Plc (Lloyds Banking Group)	£20m	AA-	F1+	364 days/Instant access
Term Deposits/ Call Accounts	UK	Barclays	£20m	AA-	F1+	364 days/Instant access
Term Deposits/ Call Accounts	UK	Clydesdale	£20m	AA-	F1+	364 days/Instant access
Term Deposits/ Call Accounts	UK	HSBC	£20m	AA	F1+	364 days/Instant access
Term Deposits/ Call Accounts	UK	Nationwide	£20m	AA-	F1+	364 days/Instant access
Term Deposits/ Call Accounts	UK	Royal Bank of Scotland	£20m*	AA-	F1+	364 days/Instant access
AAA rated Money Market Funds	UK/Ireland/ Luxembourg	Constant Net Asset Value Money Market Funds	£15m in any one institution, subject to an overall limit in MM Funds of £45m	AAA	F1+	Instant access

* Approval of this TMSS by the Council also approves the use of the Council's current banker which is Nat West Bank, part of the Royal Bank of Scotland Group. Therefore, when maximum deposits with RBS are made (£20m) this group limit could be exceeded temporarily by the current account credit balance remaining overnight with Nat West Bank. There will also be the usual daylight exposure.

NB: All of the above banks and building societies are members of the UK Government Credit Guarantee Scheme.

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

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 ▪ 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)	*6 years*	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)	✓	*6 years*	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.