Appendix 4

Treasury Management Strategy Statement and Investment Strategy 2014/15 to 2016/17

Contents

Annexes

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") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators on an annual basis. The TMSS also incorporates the Investment Strategy as required under the Communities and Local Government (CLG) Department's 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 are integral elements of treasury management activities and include Credit and Counterparty Risk, Liquidity Risk, Market or Interest Rate Risk, Refinancing Risk and Legal and Regulatory Risk.

1.4 The strategy takes into account the impact of the Council's proposed Revenue Budget and Capital Programme on the Balance Sheet position, the current and projected Treasury position, the Prudential Indicators and the outlook for interest rates. Subsequent changes to the revenue budget and capital programme will require adjustments to the TMSS and Prudential Indicators.

1.5 The purpose of this report is to propose:

- Treasury Management Strategy - Borrowing in Section 4, Investments in Section 5
- Prudential Indicators – these are detailed throughout the report and summarised in Annex 2
- MRP Statement – Section 10

2. CIPFA Treasury Management Code of Practice

2.1 Adoption of the CIPFA Treasury Management Code of Practice is one of the Prudential Indicators. The Council originally adopted the Code of Practice in May 2002. Revisions to the Code in 2009 and 2011 have been reflected in updated versions of all policies and procedures.

3. Balance Sheet and Treasury Position

3.1 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 for each pool, based on the current proposed Revenue Budget and Capital Programmes, are:

Table 1a: Treasury Position – General Fund

	31/03/2013 Actual £'000	31/03/2014 Estimate £'000	31/03/2015 Estimate £'000	31/03/2016 Estimate £'000	31/03/2017 Estimate £'000
General Fund CFR	277,726	276,252	281,727	269,122	256,227
Less: Share of existing External Debt & Other Long Term Liabilities	167,493	155,467	148,521	142,339	133,599
Internal Borrowing	110,233	120,785	115,785	110,785	105,785
Cumulative Net Borrowing Requirement	0	0	17,421	15,998	16,843

Table 1b: Treasury Position – HRA

	31/03/2013 Actual £'000	31/03/2014 Estimate £'000	31/03/2015 Estimate £'000	31/03/2016 Estimate £'000	31/03/2017 Estimate £'000
HRA CFR	271,096	271,096	271,096	299,066	314,407
Less: Share of Existing External Debt & Other Long Term Liabilities	252,887	226,646	199,903	194,657	184,405
Internal Borrowing	18,209	44,450	44,450	44,450	44,450
Cumulative Net Borrowing Requirement	0	0	26,743	59,959	85,552

3.2 The tables above show how the Council's capital requirement is funded currently and how it is expected to be funded in the coming years. Due to the differential between short and long term interest rates (discussed in more detail in section 4), the Council has maximised the amount of internal borrowing that can be done. As short term interest rates are not expected to rise over the next two years, it is anticipated that a significant level of internal borrowing will continue, with the only reduction expected reflecting the planned movement in reserves.

3.3 Ensuring that gross external debt does not exceed the CFR over the medium term is a key indicator of prudence. There has been no difficulty meeting this requirement in 2013-14 to date, nor are there any difficulties envisaged for future years, as the levels of internal borrowing in tables 1a and 1b above demonstrate.

3.4 It is a requirement for the HRA CFR to remain with the limit of indebtedness or "debt cap" set by the DCLG at the time of the implementation of self-financing. The table below shows the current expected level of the HRA CFR and the debt cap. Any decision by the Council to undertake new borrowing for housing will cause the future years' debt predictions for the HRA debt pool to increase.

Table 2: HRA Debt Cap

	31/03/2013 Actual £'000	31/03/2014 Estimate £'000	31/03/2015 Estimate £'000	31/03/2016 Estimate £'000	31/03/2017 Estimate £'000
HRA CFR	271,096	271,096	271,096	299,066	314,407
HRA Debt cap	327,538	327,538	327,538	327,538	327,538
Headroom	56,442	56,442	56,442	28,472	13,131

3.5 Table 3 below shows proposed capital expenditure over the coming three financial years. It is a requirement of the Prudential Code to ensure that capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax and housing rent levels.

Table 3: Capital Expenditure

	2012/13 Actual £'000	2013/14 Approved £'000	2013/14 Projected Out-turn £'000	2014/15 Estimate £'000	2015/16 Estimate £'000	2016/17 Estimate £'000
General	41,317	47,811	52,824	46,563	34,307	31,140
HRA	40,673	34,202	34,269	63,310	67,728	51,660
Total	81,990	82,013	87,093	109,873	102,035	82,800

3.6 Capital expenditure is expected to be financed or funded as follows:

Table 4: Capital Financing

	2012/13 Actual £'000	2013/14 Approved £'000	2013/14 Projected Out-turn £'000	2014/15 Estimate £'000	2015/16 Estimate £'000	2016/17 Estimate £'000
Capital receipts	9,608	16,073	16,947	9,269	13,679	14,757
Other grants & contributions	7,194	13,130	8,536	9,896	9,589	8,478
Government Grants	27,278	15,278	16,180	32,307	9,726	10,464
Reserves / Revenue contributions	30,941	28,657	30,779	40,044	39,271	32,413
Total Financing	75,021	73,138	72,442	91,516	72,265	66,112
Borrowing	6,969	8,875	14,652	18,357	29,770	16,688
Total	81,990	82,013	87,093	109,873	102,035	82,800

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

Table 5: Incremental Impact of Capital Investment Decisions

	2012/13 Actual £	2013/14 Approved £	2013/14 Projected Out-turn £	2014/15 Estimate £	2015/16 Estimate £	2016/17 Estimate £
Increase in Band D Council Tax	0.41	8.77	14.22	17.19	3.34	4.11
Increase in Average Weekly Housing Rents	0.09	0.13	0.12	0.17	1.85	1.60

3.8 The ratio of financing costs to the Council's net revenue stream 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 ratio is based on costs net of investment income.

Table 6: Ratio of Financing Costs to Net Revenue Stream

	2012/13 Actual %	2013/14 Approved %	2013/14 Projected Out-turn %	2014/15 Estimate %	2015/16 Estimate %	2016/17 Estimate %
General Fund	2.78	2.62	2.10	2.16	2.32	2.34
HRA	13.18	12.94	11.83	11.13	11.19	11.27

4. Borrowing Strategy

4.1 A breakdown of the Council's current and expected external borrowing plus other long-term liabilities is shown in Annex 1. This is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

4.2 The Authorised Limit sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) and is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit). The Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases. 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.

Table 7: Authorised Limit for External Debt

	2012/13 Actual Debt £'000	2013/14 Approved £'000	2013/14 Projected Out-turn £'000	2014/15 Authorised Limit £'000	2015/16 Authorised Limit £'000	2016/17 Authorised Limit £'000
Borrowing	361,702	569,256	327,159	489,334	508,442	514,754
Other Long-term Liabilities	32,270	102,037	54,954	71,745	67,545	63,345
Total	393,972	671,293	382,113	561,079	575,987	578,099

4.3 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. The Operational Boundary and Authorised Limit apply at the total level.

Table 8: Operational Boundary for External Debt

	2012/13 Actual Debt £'000	2013/14 Approved £'000	2013/14 Projected Out-turn £'000	2014/15 Operational Boundary £'000	2015/16 Operational Boundary £'000	2016/17 Operational Boundary £'000
Borrowing	361,702	469,256	327,159	359,099	408,207	444,519
Other Long-term Liabilities	32,270	68,024	54,954	66,745	62,545	58,345
Total	393,972	537,280	382,113	425,844	470,752	502,864

4.4 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 Corporate Committee.

4.5 Treasury management and borrowing strategies in particular continue to be influenced not only by the absolute level of borrowing rates but also the relationship between short and long term interest rates. The interest rate forecast provided in Annex 3 indicates that an acute difference between short and longer term interest rates is expected to continue beyond 2016. This difference creates a “cost of carry” for any new longer term borrowing where the proceeds are temporarily held as investments because of the difference between what is paid on the borrowing and what is earned on the investment.

4.6 This “cost of carry” has been a feature of money markets since 2009-10 and by essentially lending its own surplus funds to itself (i.e. internal borrowing) the Council has minimised borrowing costs and reduced overall treasury risk by reducing the level of its external investment balances. As this position is expected to continue throughout 2014-15, there are no plans to replace this internal borrowing with external borrowing. When the 2013-14 strategy was prepared it was projected that new external borrowing of approximately £80 million was required in the year to refinance maturing debt. Currently, new debt is forecast at £20 million and will comprise relatively short duration local authority borrowing to minimize interest costs. Debt maturities of £30 million in 2014-15 (including £20 million of under one year debt taken out in 2013-14) will require refinancing.

4.7 The Council will adopt a flexible approach to this borrowing in consultation with its treasury management advisers, Arlingclose Ltd. The following issues will be considered prior to undertaking any external borrowing:

- Affordability;

- Maturity profile of existing debt;
- Interest rate and refinancing risk;
- Borrowing source.

4.8 In conjunction with advice from its treasury management adviser, Arlingclose Ltd, the Council will keep under review the following borrowing options:
  - PWLB loans
  - Borrowing from other local authorities
  - Borrowing from institutions such as the European Investment Bank and directly from Commercial Banks
  - Borrowing from the Money Markets
  - Capital markets (stock issues, commercial paper and bills)
  - Structured finance
  - Leasing

4.9 The “cost of carry” discussed above has resulted in an increased reliance upon shorter dated and variable rate borrowing. These types of borrowing inject volatility into the debt portfolio in terms of interest rate risk, however this is counterbalanced by its affordability and alignment of borrowing costs with investment returns. The Council’s exposure to shorter dated and variable rate borrowing is kept under regular review by reference to the difference between variable rate and longer term borrowing costs. A narrowing in the spread by 0.5% will result in a review of the borrowing strategy in conjunction with the Council’s treasury management advisers to determine whether the exposure to shorter dated and variable rates is maintained or altered. In recent months this spread has widened rather than shortened.

4.10 The Council has £125m of loans which are LOBO loans (Lender’s Options Borrower’s Option) and all of them are in their call periods. A LOBO is called when the Lender exercises its right to amend the interest rate on the loan at which point the Borrower can accept the revised terms or reject them and repay the loan. LOBO loans present a potential refinancing risk to the Council since the decision to call a LOBO is entirely at the lender’s discretion. As LOBOs currently make up 35% of the total external debt portfolio, this is a significant risk. However, at the present time the interest rates on LOBO loans of 4.7% to 4.75% are above PWLB rates making any opportunities to repay both unlikely and financially beneficial. Any LOBO called will be discussed with the Council’s treasury advisers prior to the acceptance of any revised terms. The default position will be the repayment of the LOBO without penalty i.e. the revised terms will not be accepted.

4.11 The Council’s debt portfolio can be restructured by prematurely repaying loans and refinancing them on similar or different terms to achieve a reduction in risk and/or savings in interest costs. The lower interest rate environment and changes in the rules regarding the premature repayment of PWLB loans has adversely affected the scope to undertake meaningful debt restructuring, although occasional opportunities arise. The rationale for undertaking any debt rescheduling would be one or more of the following:

- Savings in risk adjusted interest costs
- Rebalancing the interest rate structure of the debt portfolio
- Align long term cash flow projections and debt levels
- Changing the maturity profile of the debt portfolio.

In the short term gains would accrue from replacing long term debt with shorter maturities, but from a longer term perspective this would not add value. Borrowing and rescheduling activity will be reported to Corporate Committee as part of the quarterly monitor reports.

4.12 The following Prudential Indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. 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.

4.13 The Council's existing level of fixed interest rate exposure is 98% and variable rate exposure is 2%, however it is recommended that the limits in place for 2013/14 are maintained in future to retain flexibility. At present variable rates from the PWLB compare unfavourably with short term loans from local authorities due to the additional margin charged over gilts. If LOBO loans are treated as variable, the current variable allocation is 40%.

Table 9: Fixed and Variable Interest Rate Exposure

	2013/14 Approved %	2013/14 Actual %	2014/15 Estimate %	2015/16 Estimate %	2016/17 Estimate %
Upper Limit for Fixed Interest Rate Exposure	100	98	100	100	100
Upper Limit for Variable Interest Rate Exposure	40	2	40	40	40

4.14 The Council is required to set limits on the percentage of the portfolio maturing in each of the periods set out in the table below. Limits in the following table are intended to control excessive exposures to volatility in interest rates when refinancing maturing debt. The limits have been set to reflect the current debt portfolio, and to allow enough flexibility to enable new borrowing to be taken for the optimum period. The limits apply to the combined General Fund and HRA debt pools.

Table 10: Maturity Structure of fixed rate borrowing

	Lower Limit	Upper Limit	31-Mar-14
	%	%	%
under 12 months	0%	40%	9%
12 months & within 24 months	0%	35%	2%
24 months & within 5 years	0%	35%	12%
5 years & within 10 years	0%	35%	10%
10 years & within 20 years	0%	35%	6%
20 years & within 30 years	0%	35%	4%
30 years & within 40 years	0%	35%	19%
40 years & within 50 years	0%	50%	15%
50 years & above	0%	50%	23%

5. Investment Policy and Strategy

5.1 Guidance from the Communities and Local Government Department (CLG) on Local Government Investments in England requires that an Annual Investment Strategy be set.

5.2 The Council's investment priorities are, in this order:

- security of the invested capital;
- liquidity of the invested capital;
- an optimum yield that is commensurate with security and liquidity.

5.3 Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the CLG Guidance. Instruments proposed for the Council's use within its investment strategy are contained in Annex 4 and the list of proposed counterparties is shown in Annex 5. In keeping with the strategy of maintaining low investment balances while internally borrowing, it is proposed that all investments will have a maturity of less than one year during 2014/15. 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. Investment activity will be reported to Corporate Committee as part of the quarterly reports.

5.4 Economies and money markets have improved in the recent months although confidence remains fragile and markets are prone to over react to negative news. Stronger commitments to protect the Eurozone have helped to stabilise the European banking sector. Although this backdrop supports a return to a more diversified counterparty structure, the investment strategy has to be consistent with the borrowing strategy, which is to repay debt and maximise the use of internal resources. Thus investment balances are anticipated to be of relatively low value. Given this backdrop, it is proposed to continue to limit the proposed counterparty list to UK institutions, Money Market Funds and Enhanced Cash Funds. The latter is a new class of investments, more fully discussed in annex 5. No investments will have duration of more than 12 months and in practice durations of more than 3 months are unlikely.

5.5 With all investments the Council makes there is a risk of default, so the proposed list of investments is prepared to minimise this risk by being selective about the counterparties to be used. It is proposed to continue to apply a minimum long term credit rating of A-, which is described as "high credit quality" by the rating agencies.

5.6 The Council treasury advisor recommends maximum maturities for individual counterparties and these will be considered when investing for periods longer than overnight.

5.7 All counterparties on the list are subjected to continual monitoring, in conjunction with the Council's treasury management advisers, to ensure that they continue to meet the high standard set. The range of information used to determine creditworthiness is:

- Credit ratings (long and short term and credit rating watches
- Credit Default Swaps (where quoted)
- Sovereign support mechanisms/potential support from a well-resourced parent institution
- Share prices
- Macro-economic indicators
- Corporate developments, news and articles, market sentiment.

5.8 If the monitoring reveals any concern about an institution's creditworthiness, it will be removed from the lending list with immediate effect. In normal circumstances a credit rating downgrade below the minimum criteria will not result in existing term deposits being recalled prior to contractual maturity. In any period of significant stress in the markets, the default position is for investments to be made with the Debt Management Office – either in the Debt Management Account Deposit Facility (DMADF) or UK Treasury Bills. (The rates of interest from the DMADF are below equivalent money market rates, but the returns are an acceptable trade-off for the guarantee that the Council's capital is secure). Current conditions are not considered to be "significant stress".

5.9 The Council currently has residual banking arrangements with Nat West, which is rated A-. Even if the credit rating of the Council's bank falls below the minimum of A-, it is proposed that the bank will continue to be used for short term liquidity arrangements (overnight and weekend investments) and business continuity arrangements if other arrangements are not available.

5.10 In order to diversify the investment portfolio, investments will be placed with a range of approved investment counterparties. Maximum investment levels with each counterparty are set out in Annex 5 will ensure prudent diversification is achieved.

5.11 Money Market Funds (MMFs) and Enhanced Cash Funds (ECFs) provide good diversification of underlying counterparty but may themselves be subject to withdrawal restriction. The Council will therefore seek to diversify any exposure by utilising more than one MMF or ECF unless there are significant instant access funds from other sources. The Council will also restrict its exposure to MMFs and ECFs with lower levels of funds under management and will not exceed 0.5% of the net asset value of the MMF or ECFs.

5.12 The Council is required to set an upper limit for principal sums invested for over 364 days, as required by the Prudential Code. 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. Given the current interest rate environment, the Council will not make investments for more than 364 days.

6. Use of Financial Instruments for the Management of Risks

6.1 The CIPFA Treasury Management Code of Practice requires the Council to state if and how it will use financial instruments, such as derivatives. Currently, local authorities' legal power to use derivative instruments remains unclear. The General Power of Competence enshrined in the Localism Bill is not sufficiently explicit. Consequently, the Council does not intend to use derivatives. Should this position change, the Council may develop a detailed and robust risk management framework governing the use of derivatives, but such a change in strategy would require full Council approval.

7. Housing Revenue Account Self-financing

7.1 Central Government completed the reform of the Housing Revenue Account (HRA) Subsidy system at the end of 2011/12. Local authorities are required to recharge interest expenditure and income attributable to the HRA in accordance with Determinations issued by the Department for Communities and Local Government.

7.2 The Determinations do not set out a methodology for calculating the interest rate to use in each instance. The Council is therefore required to adopt a policy that will set out how interest charges attributable to the HRA will be determined. The CIPFA Treasury Management Code of Practice recommends that authorities present this policy in the annual Treasury Management Strategy Statement.

7.3 On 1st April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long term loans borrowed will be assigned in to one pool or the other. Interest payable and other costs/income arising from long term loans (e.g. premiums and discounts on early redemption) will be charged/credited to the respective revenue account.

7.4 Differences between the value of the HRA loan pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured periodically and interest transferred between the General Fund and HRA at the net average rate earned by the Council on its portfolios of treasury investments and short term borrowing.

8. Outlook for Interest Rates

8.1 The interest rate forecast provided by the Council's treasury management adviser, Arlingclose Ltd, is attached at Annex 3. 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.

8.2 This interest rate forecast shows that UK base rate is forecast to remain at 0.5% until at least 2016. This would mean that short term rates remain significantly lower than long term rates throughout 2014/15 and beyond. As discussed in section 4, for this reason it is anticipated that cash balances will kept at a minimum throughout the financial year as the "cost of carry" will be significant for any borrowing taken before capital expenditure is incurred.

9. Balanced Budget Requirement

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

10. MRP Statement

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

10.2 The four MRP options available are:

- Option 1: Regulatory Method
- Option 2: CFR Method
- Option 3: Asset Life Method
- Option 4: Depreciation Method

10.3 MRP in 2014/15: The guidance states Options 1 and 2 may be used only for capital expenditure originally incurred when government support was available. Methods of making prudent provision for self financed expenditure include Options 3 and 4. There is no requirement to charge MRP in respect of HRA capital expenditure funded from borrowing.

10.4 It is a requirement for Council to approve the MRP statement before the start of the financial year. If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement will be put to Council at that time.

10.5 It is proposed the Council will continue to apply Option 1 (charge 4% per annum over 25 years) in respect of capital expenditure originally incurred when government support was available and Option 3 (charge over the life of the asset) in respect of all other capital expenditure funded through borrowing. MRP in respect of leases and PFI (Private Finance Initiative) schemes brought onto the Balance Sheet under the IFRS (International Financial Reporting Standards) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.

11. Other Issues

Monitoring & Reporting

11.1 Corporate Committee will receive quarterly reports on treasury management activity and performance. This will include monitoring of the prudential indicators.

11.2 It is a requirement of the Treasury Management Code of Practice that an outturn report on treasury activity is produced after the financial year end, no later than 30th September. This will be reported to Corporate Committee, shared with the Cabinet member for Finance & Carbon Reduction and then reported to full Council. Overview and Scrutiny Committee will be responsible for the scrutiny of treasury management activity and practices.

11.3 Officers monitor counterparties on a daily basis with advice from the Council's treasury management advisers to ensure that any creditworthiness concerns are addressed as soon as they arise. Senior management hold monthly meetings with the officers undertaking treasury management to monitor activity and to ensure all policies and procedures are being followed.

Training

11.4 CIPFA's Treasury Management Code of Practice 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.

11.5 Given the significant amounts of money involved, it is crucial members have the necessary knowledge to take treasury management decisions. Regular training sessions are arranged for members to keep their knowledge up to date.

Treasury Advisor

11.6 The CLG's Guidance on local government investments recommends that the Investment Strategy should state:
"Whether and, if so, how the authority uses external contractors offering information, advice or assistance relating to investment and how the quality of any such service is controlled."

11.7 The Council has appointed Arlingclose Limited as their treasury advisor, to provide information and advice about the types of investment and borrowing the Council should undertake and the counterparties that should be used. Quarterly service review meetings take place to monitor the service and the appointment is formally reviewed in accordance with the Council's Contract Standing Orders.

ANNEX 1

Detail of Treasury Position

A: General Fund Pool

	31-Mar-14 Projected £'000	31-Mar-15 Estimate £'000	31-Mar-16 Estimate £'000	31-Mar-17 Estimate £'000
Existing External Borrowing commitments:				
PWLB	58,232	54,786	52,104	46,864
Market loans	42,281	42,281	42,281	42,281
Local Authorities				
Total External Borrowing	100,513	97,067	94,385	89,145
Long Term Liabilities	54,954	51,454	47,954	44,454
Total Gross External Debt	155,467	148,521	142,399	133,599
CFR	276,252	281,727	269,122	256,227
Internal Borrowing	120,785	115,785	110,785	105,785
Cumulative Borrowing requirement	0	17,421	15,998	16,843

B: HRA Pool

	31-Mar-14 Projected £'000	31-Mar-15 Estimate £'000	31-Mar-16 Estimate £'000	31-Mar-17 Estimate £'000
Existing External Borrowing commitments:				
PWLB	123,927	117,184	111,938	101,686
Market loans	82,719	82,719	82,719	82,719
Local Authorities	20,000	0	0	0
Total External Borrowing	226,646	199,903	194,657	184,405
CFR	271,096	271,096	299,066	314,407
Internal Borrowing	44,450	44,450	44,450	44,450
Cumulative Borrowing requirement	0	26,743	59,959	85,552

ANNEX 2

Summary of Prudential Indicators

No.	Prudential Indicator	2014/15	2015/16	2016/17
CAPITAL INDICATORS				
1	Capital Expenditure	£'000	£'000	£'000
	General Fund	46,563	34,307	31,140
	HRA	63,310	67,728	51,660
	TOTAL	109,873	102,035	82,800
2	Ratio of financing costs to net revenue stream	%	%	%
	General Fund	2.16	2.32	2.34
	HRA	11.13	11.19	11.27
3	Capital Financing Requirement	£'000	£'000	£'000
	General Fund	281,727	269,122	256,227
	HRA	271,096	299,066	314,407
	TOTAL	552,823	568,188	570,634
4	Incremental impact of capital investment decisions	£	£	£
	Band D Council Tax	17.19	3.34	4.11
	Weekly Housing rents	0.17	1.84	1.60

No.	Prudential Indicator	2014/15		2015/16		2016/17	
TREASURY MANAGEMENT LIMITS							
5	Borrowing limits	£'000		£'000		£'000	
	Authorised Limit	561,079		575,987		578,099	
	Operational Boundary	425,844		470,752		502,864	
6	HRA Debt Cap	£'000		£'000		£'000	
	Headroom	56,442		28,472		13,131	
7	Upper limit – fixed rate exposure	100%		100%		100%	
	Upper limit – variable rate exposure	40%		40%		40%	
8	Maturity structure of borrowing (U: upper, L: lower)	L	U	L	U	L	U
	under 12 months	0%	40%	0%	40%	0%	40%
	12 months & within 2 yrs	0%	35%	0%	35%	0%	35%
	2yrs & within 5 yrs	0%	35%	0%	35%	0%	35%
	5 yrs & within 10 yrs	0%	35%	0%	35%	0%	35%
	10 yrs & within 20 yrs	0%	35%	0%	35%	0%	35%
	20 yrs & within 30 yrs	0%	35%	0%	35%	0%	35%
	30 yrs & within 40 yrs	0%	35%	0%	35%	0%	35%
	40 yrs & within 50 yrs	0%	50%	0%	50%	0%	50%
	50 yrs & above	0%	50%	0%	50%	0%	50%
9	Sums invested for more than 364 days	0		0		0	
10	Adoption of CIPFA Treasury Management Code of Practice	√		√		√	

ANNEX 3

Arlingclose's Economic and Interest Rate Forecast

	Mar 14	Jun 14	Sep 14	Dec 14	Mar 15	Jun 15	Sep 15	Dec 15	Mar 16	Jun 16	Sep 16	Dec 16
Base Rate	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
3 month LIBID	0.45	0.45	0.50	0.55	0.65	0.75	0.75	0.75	0.75	0.75	0.80	0.80
1 year LIBID	0.90	0.95	0.95	1.00	1.05	1.10	1.15	1.20	1.25	1.30	1.40	1.40
5 yr gilt	1.45	1.50	1.55	1.60	1.76	1.70	1.75	1.85	1.95	2.10	2.30	2.50
10 yr gilt	2.55	2.60	2.65	2.70	2.75	2.80	2.85	2.90	3.00	3.10	3.30	3.50
20 yr gilt	3.25	3.30	3.35	3.40	3.45	3.50	3.55	3.65	3.75	3.85	4.05	4.15
50 yr gilt	3.45	3.50	3.55	3.60	3.65	3.70	3.75	3.80	3.85	3.95	4.05	4.15

Underlying assumptions:

- An improvement in consumer and business sentiment has seen Q1 and Q2 2013 GDP register 0.4% and 0.7%. Growth is likely to continue to strengthen with estimates for Q3 growth close to 1%. Consumer spending remains the key driver, although this may not be sustainable given the reduction in the savings ratio.
- The unemployment rate has fallen to 7.7%. The pace of decline in this measure will be dependent on a slower expansion of the workforce than the acceleration in the economy, alongside the extent of productivity.
- The CPI rate was 2.2% in October. Regulated and administered prices are likely to keep CPI above target in the near term. In the medium term inflation is expected to come back towards the target 2%.
- The principal measure in the MPC's Forward Guidance on interest rates is the Labour Force Survey (LFS) unemployment rate. The MPC intends not to raise the Bank Rate from its current level of 0.5% at least until this rate has fallen to a threshold of 7%. It currently forecasts this level to emerge in Q3/2016.
- With improving growth statistics, the appetite for further Quantitative Easing (QE) is likely to remain small.
- House price inflation is likely to rise due to the government's Help to buy scheme, where it will guarantee up to 15% of purchasers' 95% mortgages. This could lead to a housing bubble, which in turn could come under pressure if rates were to rise quickly.
- Federal Reserve monetary policy expectations - the slowing in the pace of asset purchases ('tapering') and the end of further asset purchases - will remain predominant drivers of the financial markets. The Fed did not taper in September and has talked down potential tapering in the near term and it now looks more likely to occur in early 2014.

➢The European backstop mechanisms have lowered the risks of catastrophic meltdown. The slightly more stable economic environment at the aggregate Eurozone level could be undone by political risks and uncertainty in Italy, Spain and Portugal (doubts over longevity of their coalitions). The ECB has discussed a third LTRO, as credit conditions remain challenging for European banks.

➢The US economic recovery appears to remain on course, but the unresolved political deadlock over the debt ceiling represents a risk to activity.

➢China data has seen an improvement, easing markets fears.

➢On-going regulatory reform and a focus on bail-in debt restructuring are likely to prolong banking sector deleveraging and maintain the corporate credit bottleneck.

➢Geopolitical tensions, notably surrounding Syria, make for a less than conducive backdrop while global economies remain fragile.

➢ Our projected path for short term interest rates remains flat. Markets are still pricing in an earlier rise in rates than warranted under Forward Guidance and the broader economic backdrop. However, upside risks now weight more heavily at the end of our forecast horizon.

➢We continue to project gilt yields on an upward path through the medium term. The recent climb in yields was overdone given the soft fundamental global outlook and risks surrounding the Eurozone, China and US. Yields are slowly drifting lower after the Fed stated that tapering was not going to occur, but volatility will continue.

ANNEX 4

Counterparty Policy

The investment instruments identified for use in 2014-15 are listed below under the ‘Specified’ and ‘Non – Specified’ investment categories. Specified investments are considered low risk and relate to funds invested for up to one year. Non-specified investments normally offer the prospect of higher returns but carry higher risk and may have a maturity beyond one year. All investments are sterling denominated.

Specified Investments

Instrument	Country/ Domicile	Counterparty	Maximum Counterparty Limits £m	Maximum period of investment
Term Deposits	UK	Debt Management Account Deposit Facility (DMADF), Debt Management Office (DMO)	No limit	364 days
Gilts	UK	Debt Management Office (DMO)	No limit	364 days
Treasury Bills	UK	Debt Management Office (DMO)	No limit	364 days
Term Deposits/ Call Accounts	UK	Other UK Local Authorities	£30m per local authority	364 days
Term Deposits/ Call Accounts/ Certificates of Deposit	UK or AAA	Counterparties rated at least AA- Long Term (or equivalent)	£20m per bank or banking group	364 days
Constant Net Asset Value Money Market Funds (MMFs)	UK/Ireland/Luxembourg domiciled	AAA rated Money Market Funds	£20m per MMF*; Group limit £100m	Instant Access

Investments do not include capital expenditure as defined 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). Investment in gilts would only be undertaken on advice from the Council’s treasury management adviser.

For credit rated counterparties, the minimum criteria will be the lowest equivalent long-term ratings assigned by Fitch, Moody’s and Standard & Poor’s (where assigned).

Long-term minimum: A- (Fitch); A3 (Moody's); A- (S&P)

The Council will also take into account the range of information on investment counterparties detailed in section 5.7.

The limits stated will apply across the total portfolio operated by the Council and so incorporate both Council and Pension Fund specific investments.

The limits for the period of investment are the maximum for the categories of counterparties. Lower operational limits will apply if recommended following a review of creditworthiness.

* Limit per MMF to be no more than 0.5% of the Money Market Fund's total assets.

<u>Non- Specified Investments</u>

Instrument	**Country/ Domicile**	**Counterparty**	**Maximum Counterparty Limits £m**	**Maximum period of investment**
Gilts	UK	Debt Management Office (DMO)	£10 million	36 Months
Term Deposits/ Call Accounts	UK	Other UK Local Authorities	£30m per local authority	36 Months
Term Deposits/ Call Accounts/ Certificates of Deposit	UK	Counterparties rated at least A- Long Term (or equivalent) and NatWest Bank.	£20m per bank or banking group	364 days
Variable NAV Enhanced Cash Funds	UK/Ireland/Luxembourg domiciled	AAA - rated Funds	£5m per ECF*; Group limit £15m	Minimum Weekly Redemption

Non specified investments generally have either longer maturities than one year or weaker credit ratings than AA-, but not both.

<u>Enhanced Cash Funds</u>

The potential investment universe is wide and there are many types that Haringey does not currently utilise. One category that we would like to introduce into the portfolio is enhanced cash funds (also known as short dated bond funds). These share many of the characteristics of money market funds, which are already in use:

a) Stand alone fund, mainly a Dublin plc, that invests in bank and corporate bonds, bank deposits and other financial instruments.
b) An appointed fund manager determines which investments to hold.
c) Investment is through the purchase of units.
d) Most have an AAA credit rating.

The key difference between money market funds (MMF) and enhanced cash funds (ECF) is the latter are permitted longer maximum average maturities. A rated MMF has a maximum weighted average maturity (WAM) of 60 days, while ECF typically have 360 days WAMs and some longer. This allows them to generate a higher return from buying longer dated securities. As a consequence of the longer WAM, there are a number of differences between MMF and ECF:

a) The value of investments in ECF can vary being based on the underlying value of the investments. In a MMF, any change in value is relatively small and is reflected in the declared income.
b) MMF are dealt daily with cash moving in and out on trade date. With ECF the notice and settlement period can be up to 5 days and the funds are not suitable for intra day liquidity.
c) ECF employ a wider range of instruments and some use derivatives.

ECFs are attractive in that they offer a higher return than MMF and compared with direct investments in bonds offer high levels of diversity while maintaining an overall high quality credit exposure.

As mentioned above, most ECF have a credit rating, usually AAA. There is also a separate volatility rating that measures the sensitivity of the value of the fund to changes in interest rates. When market interest rates increase, the impact on the value of longer term investments is higher than short term investments. Despite the longer WAM, many have the lowest volatility ratings because they have strict policies on selling investments when prices change.

The attraction of ECF is the higher returns. MMF generally have net returns at present of between 0.3% and 0.5%, where as an ECF with a WAM of 360 days is currently in the range 0.75% to 1.25%.

The use of such funds has been discussed with the Council's treasury advisor who are supportive provided the exposure is limited to 20-25% of the total deposits and we invest with higher security / lower volatility funds. We will avoid funds that use derivatives as the legality of these for local authorities is unclear. Implementation will involve both a switch from MMF and DMO deposits. A maximum of £5 million invested with a single fund is proposed.

ANNEX 5

Lending List of counterparties for investments

This is the proposed list of counterparties which the Council can lend to, providing the counterparties meet the requirements set out in Annex 4 at the time of investment. The list will be kept under constant review and counterparties removed if the process described in 5.7 and 5.8 raises any concerns about their credit worthiness.

Instrument	Country/ Domicile	Counterparty	Maximum Counterparty Limit £m
Gilts, Treasury Bills, Term Deposits	UK	Debt Management Office (Term deposits with Debt Management Account Deposit Facility DMADF)	No limit
Term Deposits	UK	Other Local Authorities	£30m per local authority
Term Deposits/ Call Accounts/ Certificates of Deposit	UK	Barclays Bank Plc	20
Term Deposits/ Call Accounts/ Certificates of Deposit	UK	HSBC Bank Plc	20
Term Deposits/ Call Accounts/ Certificates of Deposit	UK	Lloyds Banking Group including Lloyds TSB and Bank of Scotland	20
Term Deposits/ Call Accounts/ Certificates of Deposit	UK	Nationwide Building Society	20
Term Deposits/ Call Accounts/ Certificates of Deposit	UK	RBS Group including Nat West Bank and Royal Bank of Scotland	20
Term Deposits/ Call Accounts/ Certificates of Deposit	UK	Standard Chartered Bank	20

The counterparty list excludes MMF and ECF's as the name of the fund reflects the fund manager not the quality of the underlying holdings. Selection of MMFs and ECFs will be based on the criteria set of in Annex 4. The limit for any single MMF is £20 million and each ECF is £5 million.