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OXFORD CITY COUNCIL

To:	**City Executive Board** **Council**
Date:	**12th February 2014** **19th February 2014**
Report of:	**Head of Finance**
Title of Report:	**TREASURY MANAGEMENT STRATEGY FOR 2014/15**

Summary and Recommendations

Purpose of report:
To present the Treasury Management Strategy for 2014/15 with the Prudential Indicators for 2014/15 – 2017/18.

Key decision? No

Executive lead member: Councillor Ed Turner

Policy Framework: Sustaining Financial Stability

Recommendation(s): City Executive Board is asked to recommend that Council:

1. Approve the Treasury Management Strategy 2014/15, and the treasury prudential indicators at paragraphs 13 – 28.
2. Approve the Investment Strategy for 2014/15 and the detailed investment criteria as set out in paragraphs 29 – 48 and appendix 1, including the changes highlighted in paragraph 9.
3. Adopt and approve the Prudential Indicators and limits for 2014/15 to 2017/18 as set out in paragraphs 50-51 and Appendix 2 below.
4. Approve the Minimum Revenue Provision (MRP) statement at paragraphs 18 – 28 which sets out the Council's policy on repayment of debt.

Appendices:
1 – Credit and Counterparty Risk Management
2 – Prudential Indicators
3 – Risk Register

Executive Summary

1. The Council's Treasury Management Strategy has been written in accordance with the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice. There are no significant changes proposed to the Treasury Management Strategy for 2014/15.

2. The report presents the Council's prudential indicators estimated for 2014/15 – 2017/18. Notable indicators include capital expenditure and borrowing limits, as these are areas of significant activity.

3. Members are required to agree the Council's Minimum Revenue Provision (MRP) policy which is the 'prudent' charge the Council will make to revenue for the repayment of debt, (paragraphs 25-27).

4. The Council's average investments during the financial year amounted to £58.2m and ranged from £40.7m to £74.3m being invested at any one time; this is an increase from the previous year when average investments were £48.1m and ranged from £35.7m to £60.3m. Cash balances have risen due to:

   - slippage in the capital program, main item being Competition Swimming pool due to legal issues (an estimated £14 million is forecast for 2013/14); and
   - Increased cash balances within the HRA arising from self-financing (the net difference between negative housing subsidy and debt financing costs is around £7 million per annum)

5. Investments are made in accordance with the Council's Treasury Management Strategy such that returns are balanced against security of investment, liquidity of cash to ensure funding of day to day cash flows, and yield.

6. The Council's external debt will reduce to £200.5m by the end of March 2014 from £201.3m. This debt is held at fixed rates, with varying periods to maturity, £198.5m relates to the Housing Revenue Account and the introduction of HRA self-financing.

7. As at 1st April 2013, the Council had one long-term variable rate loan with South Oxfordshire District Council, in respect of debt associated with the boundary change; at the beginning of 2013/14, the remaining balance on this debt was £0.9m and this has since been repaid in full.

8. The Council's Capital Programme over the next four years will be funded from a combination of government grants, capital receipts, S106 funding, and revenue resources. The costs of Prudential borrowing which all relate to the purchase of vehicles are factored into revenue budgets.

9. There are a number of minor changes to the Investment Strategy for 2014/15 previously agreed at Council as discussed in paragraph 48 including:

   - an increase in the maximum investment limit with any one bank or rated building society meeting the Council’s lending list criteria for investments up to 1 year, from £10m to £15m, however the limit of 20% of total investments remains in place
   - an increase in the maximum limit on individual categories of non-specified investments from 10% to 15%. The overall limit of a maximum of 25% of total investment portfolio in non-specified investments remains unchanged.

Economic Background

10. Despite an increase in Gross Domestic Product of 0.8% between July and Sepember 2013 being announced, the economy remains fragile. The Chancellor has insised he will hold firm with his deficit reduction policies, announcing a further £25bn fo saving to be made, and an expectation of a balanced budget by 2018/19.
11. Growth prospects remain positive looking forward although wage inflation continues to remain significantly below CPI inflation so disposbale income and living standards are under pressure. However there has been a notable decline in the unemployment rate which has forces some backtracking on the initial terms of the Bank of Engalnd Monetary Policy Committee's Forward Guidance. The accomplishment of the 7% unemployment target will not trigger an automatic hike in official interest rates. Rather, it will prompt a more focused discusion of options going forward. This trigger, however, is still thorught to be at least two years away and as a result interest rates are unlikely to rise before 2016/17.

12. The current economic outlook and structure of market interest rates and government debt yields have several key treasury mangement implications:
    - Although immediate concerns about the Eurozone have subsided, sovereign debt difficulties have not gone away and there are major concerns as to how these will be managed over the next few years. Consequently, the use of higher quality counterparties for shorter time periods remains prudent.
    - Investment returns are likely to remain relatively low during 2014/15 with latest forecasts suggesting increases from 0.70% upto 1%.
    - Borrowing rates are trending upwards. Hence the policy of avoiding new borrowing by running down cash

balances (internal borrowing) which has served well over the last few years remains.

Treasury Management Strategy

Borrowing and Debt Strategy 2014/15
Prudential Borrowing

13. Under the prudential code, individual authorities are responsible for deciding the level of their borrowing. The system is designed to allow authorities that need, and can afford to, to borrow in order to pay for capital investment.

14. The prudential system provides a flexible framework within which capital assets can be procured, managed, maintained and developed. At a strategic level it allows authorities to decide the balance between schemes that are charged through revenue and those charged through capital. The arrangements also facilitate 'invest to save' schemes where they are affordable, prudent and sustainable.

15. The parameters for determining the level of prudential borrowing are:

    - That the Council must set a balanced revenue budget that includes the revenue consequences of any capital financing i.e. the revenue budget needs to be able to cover the interest and debt repayment of any borrowing' as well as the running costs of the new project
    - That the impact of the agreed authorised borrowing limit on Council Tax or council rents is reasonable.

16. Each council must therefore take account of its local circumstances in determining its borrowing level.

17. The Draft Capital Programme includes approximately £6.2m of General Fund prudential borrowing for the purchase of vehicles over the period 2014/15 - 2017/18. The revenue impact of the borrowing is estimated at around £400k per annum and is factored into the Medium Term Financial Plan. The purchase of vehicles for service delivery outright is considered to be a cheaper option than other procurement options such as leasing due to the leasing costs and return conditions. However it is an area that the Council keeps under review.

Minimum Revenue Provision (MRP) Statement 2014/15

18. Prudential borrowing increases the Council's Capital Financing Requirement (CFR) or underlying need to borrow for financing capital expenditure. Whether the Council actually borrows to finance capital expenditure is a treasury decision unconnected to the capital

financing decision. In practice the Council is unlikely to need to borrow externally in the medium term as it has sufficient revenue balances to cover this expenditure. Nevertheless the Council is required to make a charge to its revenue account for internal borrowing. This charge is known as a Minimum Revenue Provision (MRP) and reflects the repayment of principle. Additional voluntary payments can also be made if required (Voluntary Revenue Provision (VRP)).

19. Regulations require Council to approve an MRP statement annually in advance. The recommended statement is as follows:

a) For Capital expenditure incurred before 1st April 2008 or which in the future will be Supported Capital Expenditure[1], existing practice, outlined in former DCLG regulations, will apply.

b) For all unsupported[2] borrowing incurred after1st April 2008 the MRP policy will be the Asset life method – MRP will be based on the estimated life of the assets and the borrowing charged to the revenue account in equal instalments over the life of the asset in accordance with the proposed regulations

Table 1:- Estimated General Fund MRP 2013/14 – 2017/18

	2013/14 Revised Estimate £000's	2014/15 Estimate £000's	2015/16 Estimate £000's	2016/17 Estimate £000's	2017/18 Estimate £000's
General Fund MRP	2,436	2,664	2,634	2,450	2,523
	2,436	**2,664**	**2,634**	**2,450**	**2,523**

20. There is no requirement on the HRA to make a minimum revenue provision but there is a requirement for a depreciation charge to be made. Regulations allow the Major Repairs Allowance to be used as a proxy for depreciation for the first five years of the HRA self-financing scheme after which depreciation will be calculated in accordance with proper accounting practices. Depreciation on HRA properties is estimated at £5.8m per annum and since MRA is in line with the actual depreciation charge this should not cause issues for the authority going forward.

21. The S151 Officer has delegated authority to determine the need for any future borrowing taking into account the prevailing interest rates and associated risks. A combination of long-term and short-term fixed and variable rate borrowing may be considered. This may include borrowing in advance of future years' requirements.

[1] Supported Capital Expenditure means the total amount of capital expenditure which a local authority has been notified by Government will be given as part of the grant payment
[2] Unsupported borrowing is any borrowing not covered by Government grants

22. Borrowing may be undertaken to fund the approved Capital Programme or to fund future debt maturities. The S151 Officer will adopt a cautious approach to any such borrowing and take into account the following factors:

- Ensure the on-going revenue liabilities created, and the implications for the future plans and budgets have been considered
- Evaluate the economic and market factors that might influence the manner and timing of any decision to borrow
- Consider the pros and cons of alternative forms of funding including internal borrowing
- Consider alternative sources of borrowing and interest rates available, the most appropriate periods to fund and repayment profiles to use
- Consider the impact of borrowing in advance on investment cash balances and the consequent increase in exposure to counterparty risk, and other risk, and the level of such risks given the controls in place to minimise them.

23. Council officers, in conjunction with our treasury advisors, Capita Asset Services (formerly known as Sector), monitor both prevailing interest rates and market forecasts, thereby allowing us to respond to any changes such that the manner and timing of borrowing decisions is optimised.

24. The Council had approx £201.3m of external debt with PWLB as at 1st April 2013, all of which is held at fixed rates, with varying maturity terms up to 2057. The debt is wholly related to Housing.

25. Repayments during 2013/14 will have reduced this debt figure to approx £200.5m as at 31st March 2014.

26. The Council's Capital Financing Requirement as at 1st April 2013 was above the level of external borrowing, and is an indication of the Council's underlying need to borrow to fund its capital investments and the level of internal borrowing that has been undertaken.

27. As at 31st March 2014 this position is expected to continue which indicates a potential need to borrow on the external market in the medium term, if all schemes in the proposed Capital Programme go ahead.

28. In summary there are no changes to the Council's borrowing strategy for 2014/15.

Investment Strategy 2014/15

Interest Rates

29. Average cash balances are currently @ £58.2m and have fluctuated between £40.7m and £74.3m. Deposits are made at or close to prevailing interest rates.

30. Interest rates are currently at an all-time low, with the Base Rate having been held at 0.50% since March 2009. It is forecast to remain at this level until at least October 2016 and then slowly begin to rise.

31. All existing investment deals are taken for less than 364 days although the Council's existing Treasury Management Strategy allows for the placing of placing of longer-term deals (over 364 days), with high quality counterparties, if the returns are worthwhile and within the risk parameters set by the Council. Such deals could earn around 0.5% higher returns on transactions of similar amounts placed for less than 364 days. These deals do carry an additional risk and as such are classed as non-specified investments but with interest rates forecast to remain low for the next three years officers will consider such deals within the constraints set by the existing Treasury Strategy as appropriate.

32. The primary principle governing the Council's Investment Strategy is the security of its investments; however yield or return on investment and liquidity are also key issues. Consequently, procedures determining the maximum periods fund may be invested for as well as the nature of those funds/investment types are regularly reviewed.

33. The Council aims to achieve the optimum return on its investments commensurate with proper levels of security and liquidity.

34. Investment instruments identified for use are listed in Appendix 1 under the Specified and Non-Specified investment categories. Counterparty limits are set in accordance with the Council's Treasury Management Practices (TMP's).

Creditworthiness Policy

35. The Council utilises the creditworthiness service provided by Capita Asset Services. The model combines the credit ratings, credit watches and credit outlooks from all three credit agencies – Fitch, Moody's and Standard and Poors in a weighted scoring system which is then combined with an overlay of Credit Default Swap[3] spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour

[3] A financial swap agreement that the seller of the CDS will compensate the buyer in the event of a loan default

codes are used by the Council to determine the duration of investments. The Council is satisfied that this service gives an improved level of security for its investments. It is also a service which the Council would not be able to replicate using in house resources.

36. The Council is alerted to changes to ratings of all three agencies through its use of the Capita Asset Services creditworthiness service and takes the following action in respect of this update :

- if a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- if a counterparty's credit rating is placed on negative watch or negative outlook, officers carry out a review to determine whether the institution is still worthy of inclusion on the Council's treasury management lending list. If there is any doubt, the institution is temporarily suspended pending the credit rating agency's full review.

In addition to Capita Asset Services, the Council also uses other market data on government support for banks and the credit rating of that government support to inform its investment decisions and information in movements in Credit Default Swaps against the iTraxx benchmark and other market data on a weekly basis

37. The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA- from Fitch Ratings (or equivalent from other agencies if Fitch does not provide)

38. For operational purposes, the Council's counterparty list is reviewed on a daily basis taking into account market information and changes to the criteria provided. This list is maintained by the Treasury team, and reported to the Section 151 Officer on a regular basis.

39. Within the agreed Investment Strategy the S151 Officer has delegated powers to undertake the most appropriate form of investments depending on prevailing interest rates and the security of the counterparty at the time.

40. The Council also retains the option to place deposits with the top five Building Societies by size of asset base, which is a deviation from Capita Asset Services' criteria. Only Building Societies with an asset base of £9bn or above are included on the treasury management lending list. Lending is restricted to a maximum of £3mand 3 months per Building Society. In addition to this, the total invested with these Building Societies is restricted to a maximum of 20% of the overall average investment total.

41. There are currently five Building Societies which have an asset base of over £9bn as shown below:

Table 2 Building Society Counterparties ranked by Asset Size

Building Society	Asset Base*	Year End
Nationwide	£190,718m	31st March 2013
Yorkshire	£33,497m	31st March 2013
Coventry	£26,934m	31st March 2013
Skipton	£13,760m	31st March 2013
Leeds	£10,315m	31st March 2013

* Source: KPMG Building Societies Database 2013

42. Limits have also been placed on countries and sectors, as follows:

- No more than 20% of the previous year's average monthly investment balance with any one counterparty or group (currently £12.2m)
- No limit for UK investments
- Maximum 10% of total investments to be with institutions in other countries that meet the current criteria

43. The Council's banking services are currently provided by the Co-operative Bank. The credit ratings for this bank do not currently meet the criteria set out above and therefore, the Council only uses the Co-operative for transactional purposes only. This is intended to limit the Council's risk.

44. In November 2013, the Co-operative announced that whilst it would honour existing contracts with local authority customers; it would not be renewing them. The Council's current contract is due to expire in March 2016. A re-tendering process is likely to take between six and twelve months and on the basis that as the Co-operative wind down their operation less support will be available to the Council, officers are scheduling a project to procure a revised banking service with effect from 1st April 2015. We may co-operate with other local authorities on this procurement exercise.

Specified and Non Specified Investments

45. In approving the overall investment strategy Members are approving the types of investments used. Investments are classified as either Specified or Non Specified investments and are shown in more detail in Appendix 1.

46. **A Specified investment** is one that is in Sterling, no more than 1 year in duration or, if in excess of 1 year repayment can be made within that period if wished with quality counterparties meeting Councils minimum credit rating criteria. **Non specified investments** are any other type of investment including those with non- rated

building societies. Whilst generally these investments will earn a higher return they are inherently more risky in nature and a maximum level of 25% of the council's total portfolio is placed on such investments.

47. Whilst there are no changes to the types of specified and non-specified investments given the increasing cash position of the Council there are some changes to the limits placed in certain types including :

- To provide additional flexibility within Non specified investments, it is recommended that the maximum % of total investments with any one type of investment increases from 10% to 15%. The previously agreed limit of 25% of the total investment portfolio with non-specified investments remains in place.
- Increasing the investment limit for banks and rated building societies is increased from £10m to £15m; this will generate a higher rate of return without increasing risk and is in line with current recommendations from Capita Asset Services. investment opportunities.

48. Members should also note that as cash balances increase Officers will look to make use of the whole range of counterparties included within the existing Treasury Management including :

- **The use of longer-term instruments** (greater than one year from inception to repayment). These instruments will only be used where the Council's liquidity requirements are safeguarded. The majority of longer-term investments are likely to be placed with other authorities and commissioning bodies although they may also include some banks if they meet the criteria set out by Capita Asset Services.
- **Direct Investment property purchases**. The Council can also consider purchasing additional investment properties to be included within the Council's investment property portfolio. The current portfolio of £86m gives a yield of approximately £6 million per annum. These properties do not directly form part of the Treasury Strategy but would provide a rate of return to the Council. Any future prospective purchases would utilise the surplus core cash and would be subject to a robust business case submitted to Council.
- **Property Funds**. Property funds are a vehicle for investing funds and diversifying investments. The Council has already made £3million of investments within these types of funds, and is currently reviewing the options for further investments. Property funds should be seen as a medium to long term investment (10 -15 years minimum) to ensure that the full benefit of the return is seen, and to also ensure that any entry and exit costs are covered over the life of the

investment. Any fund of this nature incurs costs, and these vary depending on the type of fund. Property funds can provide a regular return on the initial investment amount; our current fund for instance provides a return of around 6%. In addition to this the market value of the properties and the unit price held by the Council can fluctuate. The unit price can fluctuate upwards as well as downwards and variations between purchase price and latest valuation at the 31st March or date of sale do need to be reflected in the Council's revenue account.

Icelandic Bank Investments

49. The Council placed deposits with two Icelandic banks prior to their collapse in 2009. Original balances were £3m with Heritable and £1.5m with Glitnir. Heritable has repaid 94% of the initial deposit plus interest and continue to make repayments. It is still expected that the Council will receive up to 100% back. The Council has also received over 80% of the original deposit with Glitnir. The remaining balance is currently held in Iceland, under Icelandic law, and the Council is seeking advice from Bevan Brittan, our solicitors acting on the behalf of all local authorities, and the Local Government Association regarding its options on this matter.

Prudential Indicators

50. The Council is required to set a number of indicators, relating to the affordability and prudence of its treasury activities. These indicators are all detailed In Appendix 2 , and should be monitored and reported on an annual basis.
51. The Council has met all of the prudential indicators for 2013/14 and has set out its plans for them in 2014/15 through to 2017/18.

Legal Implications

52. This report fulfils four key legislative requirements:

- The reporting of the prudential indicators setting out the expected capital activities (as required by the CIPFA Prudential Code for Capital Finance in Local Authorities). The treasury management prudential indicators are now included as treasury indicators in the CIPFA Treasury Management Code of Practice
- Agreeing the Council's Minimum Revenue Provision (MRP) policy, which sets out how the Council will pay for capital assets through revenue each year (as required by Guidance under the Local Government and Public Involvement in Health Act 2007)

- Agreeing the treasury management strategy, which sets out how the Council's treasury service will support the capital decisions taken, the day to day treasury management and the limitations on activity through treasury prudential indicators. The key indicator is the Authorised Limit, the maximum amount of debt the Council could afford in the short term, but which would not be sustainable in the longer term. This is the Affordable Borrowing limit required by S3 of the Local Government Act 2003. This is in accordance with the CIPFA code of Practice on Treasury Management and the CIPFA Prudential Code
- Agreeing the investment strategy, which sets out the Council's criteria for choosing investment counterparties and limiting exposure to the risk of loss. This strategy is in accordance with the DCLG investment guidance.

53. The Local Government Act 203 (the Act) and supporting regulations require the Council to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

54. The Constitution requires the Strategy to be reported to the City Executive Board and Full Council outlining the expected treasury activity for the forthcoming 4 years on an annual basis.

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List of background papers:
Version number: 2

APPENDIX 1

Management Practice (TMP) 1 – Credit and Counterparty Risk

Management

The CLG issued Investment Guidance in 2010, and this forms the structure of the Council's policy below.

The key intention of the Guidance is to maintain the current requirement for Councils to invest prudently, and that priority is given to security and liquidity before yield. In order to facilitate this objective the guidance requires this Council to have regard to the CIPFA publication *Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes*. This Council has adopted the Code and will apply its principles to all investment activity. In accordance with the Code, the Section 151 Officer has produced its treasury management practices (TMPs). This part, TMP 1, covering investment counterparty policy requires approval each year.

Annual Investment Strategy - The key requirements of both the Code and the investment guidance are to set an annual investment strategy, as part of its annual treasury strategy for the following year, covering the identification and approval of the following:

- The strategy guidelines for choosing and placing investments, particularly non-specified investments.
- The principles to be used to determine the maximum periods for which funds can be committed.
- Specified investments the Council will use. These are high security (i.e. high credit rating, although this is defined by the Council, and no guidelines are given), and high liquidity investments in sterling and with a maturity of no more than a year.
- Non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and a limit to the overall amount of various categories that can be held at any time.

The investment policy proposed for the Council is:

Strategy Guidelines – The main strategy guidelines are contained in the body of the treasury strategy statement.

Specified Investments – These investments are sterling investments that do not exceed a maturity period of more than one year, or those which could be for a longer period but where the Council has the right to be repaid within twelve months if it wishes. These are considered low risk assets where the possibility of loss of principal or investment income is small. These would include sterling investments which would not be defined as capital expenditure with:

1. The UK Government (such as the Debt Management Account deposit facility, UK Treasury Bills or Gilts with less than one year to maturity).
2. Supranational bonds of less than one year's duration.
3. A Local Authority, Parish Council, Community Council, Fire or Police Authority
4. Pooled investment vehicles (such as money market funds) that have been awarded a high credit rating by a credit rating agency. For category 4, this covers pooled investment vehicles, such as money market funds, rated AAA by Standard and Poor's, Moody's or Fitch rating agencies.
5. A body that is considered of a high credit quality (such as a bank or building society) meeting the minimum 'high' quality criteria where applicable.

Within these bodies, and in accordance with the Code, the Council has set additional criteria to set the time and amount of monies which will be invested in these bodies.

These criteria are:

	Minimum credit criteria/colour banding	**Max % of total investments /£ limit per institution**	**Max maturity period**
DMADF – UK Government	Not applicable	100%	364 days
UK Government Gilts	UK Sovereign rating	20%	364 days
UK Government Treasury Bills	UK Sovereign rating	20%	364 days
Bonds issued by multilateral development banks	UK Sovereign rating	20%	6 months
Money Market Fund	AAA	£20m	Liquid
Local Authorities, Fire and Police Authorities		100%	364 days
Term deposits with banks and rated building societies	Blue Orange Red Green	£15m or 20% of total investments	Up to 1 year Up to 1 year Up to 6 Months Up to 100 days
CDs or corporate bonds with banks and building societies	Blue Orange Red Green	£10m or 20% of total investments	Up to 1 year Up to 1 year Up to 6 Months Up to 100 days
Enhanced Cash funds		20%	6 months

Corporate bond funds		20%	6 months
Gilt Funds	UK sovereign rating	20%	6 months

Non-Specified Investments – Non-specified investments are any other type of investment (i.e. not defined as Specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below. Overall non specified investments will not exceed more than 25% of the investment portfolio. As the Council's average investment balance increases over the medium term decisions will need to be made on the viability of undertaking additional non specified investments. Non specified investments would include any sterling investments with:

	Minimum Credit Criteria	**Max % of total investments/£ limit per institution**	**Max maturity period**
Local Authorities, Fire and Police Authorities		15% of total investments	Up to 2 years
Fixed term deposits with variable rate and variable maturities	Orange	15% of total investments	Up to 1 year
Fixed term deposits with variable rate and variable maturities	Yellow Purple	£10m or 20% of total investments	Up to 5 years Up to 2 years
Commercial paper issuance covered by a specific UK Government (explicit) guarantee		10% of total investments	Up to 1 year
Fixed term deposits with unrated Building Societies	Asset Base over £9bn	£3m – 20% of total investments	100 days
Commercial paper other		15% of total investments	Up to 1 year
Corporate bonds		15% of total investments	Up to 1 year
Other debt issuance by UK banks covered by UK Government (explicit) guarantee		15% of total investments	Up to 1 year
Floating rate notes		15% of total investments	Up to 1 year
Housing Associations		15% of total investments	Medium to long term
Property funds		15% of total investments	Medium to long term

The Monitoring of Investment Counterparties - The credit rating of counterparties will be monitored regularly. The Council receives credit rating information (changes, rating watches and rating outlooks) from Capita Asset Services on a weekly basis, and counterparties are checked promptly. On occasion ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately by the Head of Finance, and if required new counterparties which meet the criteria will be added to the list.

APPENDIX 2

Prudential Indicators

Prudence

A. Capital Expenditure Plans

55. The Council's capital expenditure plans are the key driver of treasury management activity. Estimates of capital expenditure for the period 2014/15 to 2017/18 are summarised below and this forms the first of the prudential indicators. The revenue consequences of associated borrowing and any on-going maintenance costs are accommodated within the Council's revenue budgets.

56. Capital expenditure can be paid for immediately, by applying capital resources such as capital receipts, capital grants, external funding or revenue contributions, but if these resources are insufficient any residual expenditure will be undertaken by Prudential Borrowing and will add to the Council's borrowing need, or Capital Financing Requirement (CFR).

57. Estimates of resources such as capital receipts may be subject to uncertainty i.e. anticipated asset sales may be postponed or reduced due to the property market or planning issues.

58. Elsewhere on the agenda the proposed Capital Programme is recommended for approval, a summary of these figures is in the table below, showing the capital expenditure and how it will be financed. Any shortfall of financing results in a borrowing need.

Table 3:-Capital Expenditure and Financing

	2013/14 Revised Estimate £000's	2014/15 Estimate £000's	2015/16 Estimate £000's	2016/17 Estimate £000's	2017/18 Estimate £000's
Expenditure					
General Fund	18,339.3	31,189.0	14,035.9	8,163.3	2,302.0
HRA	14,386.0	21,387.0	18,070.0	19,140.0	20,113.0
Total expenditure	**32,725.3**	**52,576.0**	**32,105.9**	**27,303.3**	**22,415.0**
Financed by:					
Developer Contributions	938.2	683.0	555.9	500.0	450.0
Capital Grants	2,898.8	7,522.0	872.0	597.0	447.0
Capital Receipts	12,086.9	8,975.5	6,506.7	4,023.0	1,405.0
Revenue	14,059.8	32,488.8	22,116.2	21,360.0	19,261.0
Prudential Borrowing (Vehicles)	2,741.6	2,906.7	2,055.1	823.3	852.0
Total funding	**32,725.3**	**52,576.0**	**32,105.9**	**27,303.3**	**22,415.0**

B. Capital Financing Requirement (CFR).

59. The CFR is the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is

essentially a measure of the Council's underlying need to borrow. Prudential borrowing is explored in more detail below.

60. The CFR includes any other long term liabilities (eg finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes.

Table 4:- Capital Financing Requirement

	2013/14 Estimate £000's	2013/14 Revised Estimate £000's	2014/15 Estimate £000's	2015/16 Estimate £000's	2016/17 Estimate £000's	2017/18 Estimate £000's
General Fund	1,324	13,808	13,650	13,021	12,217	10,546
HRA	222,297	204,300	204,300	204,300	204,300	204,300
	223,621	218,108	217,951	217,321	216,517	214,846
Movement in CFR	-1,739	-7,252	-157	-630	-804	-1,671
Prudential Borrowing			2,907	2,055	823	852
MRP			-3,064	-2,685	-1,627	-2,523

Affordability

61. The Strategy also includes the Prudential Indicators, which the authority is required to consider before determining its budget and treasury management arrangements for the new financial year. These indicators are a statutory requirement and therefore have to be reported to Council each year. These indicators are split into two categories the first is affordability. The affordability indicators are listed below:

C. Ratio of financing costs to the net revenue stream

62. This indicator represents the estimate of the ratio of financing costs to the net revenue stream for HRA and General Fund .

Table 5:- Ratio of financing costs to net revenue stream

	2013/14 Original Estimate £000's	2013/14 Revised Estimate £000's	2014/15 Estimate £000's	2015/16 Estimate £000's	2016/17 Estimate £000's	2017/18 Estimate £000's
General Fund	13.0%	12.2%	11.3%	11.3%	8.7%	3.5%
Housing Revenue Account	16.1%	18.5%	17.6%	16.7%	16.3%	15.5%

D. Incremental impact of capital investment decisions on Council Tax and Rents

Council Tax

63. The estimate of the incremental impact of capital investment decisions on the Council Tax is shown below; this shows the impact of any decisions that are made on investment through the Capital Programme and how it affects the Band D Council Tax.

64. The figures in Table 6 below have been calculated by looking at those schemes that are uncommitted in the current Capital Programme and looking at the impact they will have on Council Tax after taking into account capital receipts and revenue contributions.

65. The Council will not enter into any uncommitted capital scheme until the source of funding is confirmed, e.g. Capital receipts, grants, S106 or prudential borrowing. This will ensure we can avoid any unplanned revenue consequences as a result of capital expenditure.

Table 6:- Impact of Capital Expenditure on Council Tax

	2013/14 Original Estimate £	2013/14 Revised Estimate £	2014/15 Estimate £	2015/16 Estimate £	2016/17 Estimate £	2017/18 Estimate £
Overall net impact on Council Tax Band D per week	0.73	0.37	0.72	0.32	0.19	0.05

Housing Rents

66. The estimated incremental impact of capital investment decisions on weekly housing rents is shown in Table 7 below. The figures have been calculated by looking at those schemes that are currently in the Capital Programme and deducting alternate funding resources.

67. The key drivers for setting housing rents with effect from 1st April 2014 will be affordability and the need to cover net expenditure (including the take on of the buyout debt). Formula rent guidance states that for 2014/15 this will be inflation plus 0.5% + £2. Government are currently consulting on the level from 2015/16 onwards, indicating it may be linked to CPI + 1.0%.

68. Since all the HRA Capital Programme is financed from revenue and capital receipts the effect on council rents is as follows:

Table 7:- Impact of Capital Expenditure on Housing Rents

	2013/14 Original Estimate £	2013/14 Revised Estimate £	2014/15 Estimate £	2015/16 Estimate £	2016/17 Estimate £	2017/18 Estimate £
Overall net impact on Weekly Housing Rents	2.63	1.83	2.63	2.22	2.35	2.47

E. Authorised limit for external debt

69. This represents a limit beyond which external debt is prohibited. It reflects the level of external debt, which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Table 8:- Authorised Limit for external debt

	2013/14 Estimate £000's	2014/15 Estimate £000's	2015/16 Estimate £000's	2016/17 Estimate £000's	2017/18 Estimate £000's
General Fund	5,000	4,000	2,000	2,000	2,000
HRA	243,000	243,000	243,000	243,000	243,000
Other Long Term Liabilities	1,000	0	0	0	0
Total	249,000	247,000	245,000	245,000	245,000

70. Separately, the Council is also limited to a maximum HRA CFR through the HRA self-financing regime. These limits are:

Table 9 HRA Capital Financing Requirement

HRA Debt Limit	2013/14 Estimate £000's	2014/15 Estimate £000's	2015/16 Estimate £000's	2016/17 Estimate £000's	2017/18 Estimate £000's
Total	242,199	242,199	242,199	242,199	242,199

F. Operational boundary for external debt

71. This is based on the expected maximum external debt during the course of the year, it is not a limit, and actual external debt can vary around this boundary for short times during the year.

Table 10:- Operational boundary for external debt

	2013/14 Estimate £000's	2014/15 Estimate £000's	2015/16 Estimate £000's	2016/17 Estimate £000's	2017/18 Estimate £000's
Borrowing	3,000	2,000	0	0	0
Additional HRA Settlement	234,000	234,000	234,000	234,000	234,000
Other Long Term Liabilities	1,000	0	0	0	0
Total	238,000	236,000	234,000	234,000	234,000

G. Net Borrowing Compared to the Council's Capital Financing Requirement

72. Table 10 below shows the Council's net borrowing position compared to its Capital Financing Requirement. As can be seen, the figures show that the Council is currently borrowing below its financing requirement which indicates a need to borrow in the short to medium term. The Council needs to ensure that its total borrowing net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2014/15 and the next two financial years. This allows some flexibility for limited early borrowing for future years.

Table 11:- Net borrowing compared to CFR

	2013/14 Original Estimate £000's	2013/14 Revised Estimate £000's	2014/15 Estimate £000's	2015/16 Estimate £000's	2016/17 Estimate £000's	2017/18 Estimate £000's
Gross Borrowing	200,638	201,368	200,638	199,908	198,528	198,528
Other Long Term Liabilities	607	889	0	0	0	0
Total Gross Debt 31 March	**201,245**	**202,257**	**200,638**	**199,908**	**198,528**	**198,528**
CFR	223,621	218,108	217,951	217,321	216,517	214,846
Net Borrowing v CFR	**22,376**	**15,851**	**17,313**	**17,413**	**17,989**	**16,318**

H. Compliance with the CIPFA Code of Practice for Treasury Management in the Public Sector

73. The Council can confirm that it has complied with this code throughout 2013/14 and will continue to do so.

I. Upper limit on fixed and variable interest rate borrowing and investments

74. The purpose of this and the following two prudential indicators is to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. This indicator identifies the maximum limit for fixed interest rates based upon the debt position net of investments.

Table 12:- Upper limit on borrowing and investments

	2013/14 Estimate %	2014/15 Estimate %	2015/16 Estimate %	2016/17 Estimate %	2017/18 Estimate %
Upper limit on fixed rate borrowing	100	100	100	100	100
Upper limit on fixed rate investments	100	100	100	100	100
Upper limit on variable rate borrowing	100	100	100	100	100
Upper limit on variable rate investments	100	100	100	100	100

J. Upper and Lower limit for the maturity structure of borrowing

75. These are used to reduce the Council's exposure to large fixed rate sums falling due for repayment at the same time.

Table 13:- Upper and lower limit on borrowing maturity

	2013/14 Estimate Upper %	2013/14 Estimate Lower %	2014/15 Estimate Upper %	2014/15 Estimate Lower %	2015/16 Estimate Upper %	2015/16 Estimate Lower %	2016/17 Estimate Upper %	2016/17 Estimate Lower %	2017/18 Estimate Upper %	2017/18 Estimate Lower %
< 12 months	30	0	30	0	30	0	30	0	30	0
12 months - 2 years	30	0	30	0	30	0	30	0	30	0
2 - 5 years	80	0	80	0	80	0	80	0	80	0
5 - 10years	100	0	100	0	100	0	100	0	100	0
10 years +	100	0	100	0	100	0	100	0	100	0

76. Upper limit for principle sums invested for periods longer than 364 days; this indicator is used to reduce the need for early sale of an investment, and is based on the availability of funds after each year end. This has been set at zero due to the uncertainty of the market and reducing the risk posed by longer term investments.

Table 14:- Upper limit for investments longer than 364 days

	2013/14 Estimate %	2014/15 Estimate %	2015/16 Estimate %	2015/16 Estimate %	2016/17 Estimate %	2017/18 Estimate %
upper limit for investments for periods longer than 364 days	20	20	20	20	20	20