

The Treasury Management Strategy, Prudential Indicators 2010/11 and Annual Investment Strategy 2010/11 and Performance for 2009/10

Audit Committee

Date: 22nd June 2010

APPENDIX 1 - Adoption of the revised CIPFA Treasury Management Code of Practice 2009

INTRODUCTION

The CIPFA Code of Practice on Treasury Management in Local Authorities was last updated in 2001 and has been revised in 2009 in the light of the default by Icelandic banks in 2008. The revised Code requires that a report be submitted to the council, board or other appropriate body, setting out four amended clauses which should be formally passed in order to approve adoption of the new version of the Code of Practice and Cross-Sectoral Guidance Notes.

The revised Code also includes an amended version of the treasury management policy statement (TMPS) incorporating just three clauses and a revised definition of treasury management activities. The Code does not require this statement to be approved by the council, board or other appropriate body.

The revised Code has also set out various requirements which have been summarised in paragraph 1.4 of the Report.

RESOLUTIONS

CIPFA recommends that all public service organisations adopt, as part of their standing orders, financial regulations, or other formal policy documents appropriate to their circumstances, the following four clauses. A commentary is provided in italics on Swindon Borough Council's current degree of compliance with each clause.

1. This organisation 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 (TMPs), setting out the manner in which the organisation 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 TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of this organisation. Such amendments will not result

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in the organisation materially deviating from the Code's key principles.

Swindon Borough Council complies with this clause. Our treasury management policy statement is included as Appendix 2 to this report and treasury management practices have been adopted and are available from the Director of Finance..

2. This organisation (i.e. full 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 TMPs.

Swindon Borough Council complies with this clause. Reports are made to Council, through Cabinet, on a regular basis.

3. This organisation delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to a responsible body or Committee (being Cabinet), and for the execution and administration of treasury management decisions to as responsible officer (being the Director of Finance), who will act in accordance with the organisation's policy statement and TMPs and, if he/she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

Swindon Borough Council complies with this clause. Reports are made to Council, through Cabinet, on a regular basis.

4. This organisation nominates a responsible body or Committee (such as Audit Committee) to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

Swindon Borough Council does not completely comply with this clause. Although the remit of the Audit Committee includes both financial and risk management, there is no specific mention of Treasury Management. It is therefore recommended that this be clarified in the Council's constitution.

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APPENDIX 2 Treasury Management Policy Statement

This organisation

- defines its treasury management activities as: “The management of the authority’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks”.
- regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.
- acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.”

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APPENDIX 3 - Treasury Management scheme of delegation

(i) Full board/council

- receiving and reviewing reports on treasury management policies, practices and activities
- approval of annual strategy.

(ii) Boards/committees/council/responsible body

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices
- budget consideration and approval
- approval of the division of responsibilities
- receiving and reviewing regular monitoring reports and acting on recommendations
- approving the selection of external service providers and agreeing terms of appointment.

(iii) Body/person(s) with responsibility for scrutiny

reviewing the treasury management policy and procedures and making recommendations to the responsible body.

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APPENDIX 4 - The Treasury Management role of the Section 151 officer

The S151 (responsible) officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit recommending the appointment of external service providers.

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APPENDIX 5 – Reporting Requirements

Area of Responsibility	Council/ Committee/ Officer	Frequency
Treasury Management Policy Statement (revised)	Full Council via Cabinet	Initial adoption in 2010
Treasury Management Strategy / Annual Investment Strategy / MRP policy	Full Council via Cabinet	Annually before the start of the year
Treasury Management Strategy / Annual Investment Strategy / MRP policy – mid year report	Full Council via Cabinet	Mid year
Treasury Management Strategy / Annual Investment Strategy / MRP policy –	Full Council via Cabinet	Annually - updates or revisions at other times
Annual Treasury Outturn Report	Full Council via Cabinet	Annually by 30 September after the end of the year
Treasury Management Monitoring Reports	Cabinet	Quarterly
Treasury Management Practices	Full Council via Cabinet	Annually
Scrutiny of treasury management strategy	Audit Committee	At least annually before the start of the year
Scrutiny of treasury management performance	Audit Committee	At least annually

Further information on the subject of this report can be obtained from Paul Smith on *Direct Dial No. 01793 463976* or Email psmith2@swindon.gov.uk.

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APPENDIX 6 – TREASURY MANAGEMENT STRATEGY 2010/11

1. TREASURY LIMITS FOR 2010/11 TO 2012/13

- 1.1. It is a statutory duty under Section 3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the “Affordable Borrowing Limit”. The “Authorised Limit” is the term used in the Prudential Code to represent this limit.
- 1.2. The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax and council rent levels is ‘acceptable’.
- 1.3. Whilst termed an “Affordable Borrowing Limit”, the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years.

2. PRUDENTIAL INDICATORS FOR 2010/11 – 2012/13

- 2.1. Councils are required to set Prudential Indicators covering a 3 year period for capital expenditure, external debt and treasury management in accordance with Part 1 of the Local Government Act 2003 and the Prudential Code for Capital Finance produced by CIPFA. These are designed to support and record local decision making and to determine the impact of forward plans, rather than act as a comparison between Local Authorities. The indicators and further information around them are contained at Appendix 5.
- 2.2. The Council is also required to indicate if it has adopted the CIPFA Code of Practice on Treasury Management. This was originally adopted on 10th April 2002 by the full Council.

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3. CURRENT PORTFOLIO POSITION

3.1. The Council's treasury portfolio position at 31st December 2009 was:

	31 st March 2009		31st Dec 2009	
	Principal	Pool Avge. Rate	Principal	Pool Avge. Rate
	£m	%	£m	%
Borrowing				
Fixed rate funding - PWLB	85.5		73.1	
Variable rate funding - Market	0.0		30.0	
Temporary – market	0.0		0.0	
Total External Debt	85.5	4.86	103.1	4.56
Investments				
Managed In-house	34.5	2.72	40.0	1.28
Managed Externally	24.5	7.21	36.8	1.63
Total Investments	59.0	4.58	76.8	1.45

3.2. Long term borrowing has been undertaken twice so far in 2009/10, both in the form of "LOBO's" (Lenders Option Buyers Option). These are loans structured in such a way that after a fixed period the bank may increase the interest rate payable on the loan. The Council has at that point the option to reject the rate increase and repay the loan in full. The 2 transactions that took place were both through the Royal Bank of Scotland

3.2.1. Loan of £10m drawdown on 16/11/09 an initial rate equivalent to LIBOR Flat for 36 months (c0.6% currently), followed by a further 27 years at a fixed rate of 4.20%, with an annual option after 3 years

3.2.2. Loan of £20m drawdown on 24/11/09 at an initial rate equivalent to LIBOR Flat (capped at 4.25%) for 36 months, followed by a further 47 years at a fixed rate of 4.35%, with an annual option after 3 years

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3.3. The in-house investment return to the end of December 2009 was 1.45%, exceeding the “benchmark” 7-day rate of 0.39% by 1.06%. In order to manage the peaks and troughs of the Council’s monthly cash flow an amount of approximately £20 million will be retained in business reserve accounts for a part of each month. These funds are available either on instant access or seven days’ notice. The present strategy for any further cash surplus is to lend for as long a period as

possible within the constraints of the Council’s cash flow position and Treasury Management Policies (currently a maximum of 6 months).

3.4. The return for Investec, the single external fund manager, for the 9 months to the end of December 2009 was 1.63%,. This is well above the “benchmark” 7-day rate of 0.39%.

4. BORROWING REQUIREMENT

4.1. The Council is estimated to have a long term borrowing requirement of £38.5m in 2010-11, which comprises a new borrowing requirement of £31.5m and Replacement Borrowing of £7m .

4.2. Any approval of further capital schemes financed from borrowing will increase these figures.

4.3. The most significant cost pressure within the 2010/11 Budget which results in a net increase over 2009/10 of £1.956m

- An increase in the Minimum Revenue Provision due to the impact of increased borrowing undertaken to finance the capital programme, a substantial element relating to the substantial reduction in expected levels of capital receipts;
- The impact of capitalised Equal Pay costs;
- A further reduction in Investment income due to historically low rates and the expiry of longer term, higher rate investments.

5. PROSPECTS FOR INTEREST RATES

5.1. The Council has appointed Sector Treasury Services as treasury adviser to the Council and part of their service is to assist the Council to formulate a view on interest rates.

5.2. Sector Bank Rate forecasts for financial year ends (March) are:

- 2010 0.50%
- 2011 1.50%
- 2012 3.50%
- 2013 4.50%

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5.3. There is downside risk to these forecasts if recovery from the recession proves to be weaker and slower than currently expected.

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6. BORROWING STRATEGY

6.1. The Sector forecast for PWLB borrowing rates is as follows:

	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13
Bank rate	0.50%	0.50%	0.75%	1.00%	1.50%	2.25%	2.75%	3.25%	3.50%	3.75%	4.25%	4.25%	4.50%
5yr PWLB rate	3.05%	3.20%	3.30%	3.40%	3.60%	3.85%	4.15%	4.55%	4.60%	4.80%	4.80%	4.85%	4.85%
10yr PWLB rate	4.00%	4.05%	4.15%	4.30%	4.45%	4.60%	4.80%	4.90%	5.00%	5.10%	5.10%	5.15%	5.15%
25yr PWLB rate	4.55%	4.65%	4.70%	4.80%	4.90%	5.00%	5.05%	5.10%	5.20%	5.30%	5.30%	5.35%	5.35%
50yr PWLB rate	4.60%	4.70%	4.75%	4.90%	5.00%	5.10%	5.15%	5.20%	5.30%	5.40%	5.40%	5.45%	5.45%

- Rates are expected to gradually increase during the year, so it should therefore be advantageous to time new long term borrowing for the earlier part of the year
- Variable rate borrowing is expected to be cheaper than long term borrowing and will therefore be attractive throughout the financial year compared to taking long term fixed rate borrowing.
- PWLB rates on loans of less than ten years duration are expected to be substantially lower than longer term PWLB rates offering a range of options for new borrowing which will spread debt maturities away from a concentration in long dated debt.
- There is expected to be little difference between 25 year and 50 year rates thus loans in the 25-30 year periods could be seen as being more attractive than 50 year borrowing as the spread between the PWLB new borrowing and early repayment rates is considerably less which would maximise the potential for debt rescheduling and allow the Council to rebalance its debt maturity profile if need be.
- Significant consideration will also be given to the differential between borrowing and investment rates as although long term rates are historically very attractive, the carrying cost of these loans, which would fall on the revenue budget, is high due to extremely low investment rates.

6.3. Sensitivity of the forecast – In normal circumstances the main sensitivities of the forecast are likely to be the two scenarios noted below. The Council officers, in conjunction with the treasury advisers, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

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- if it were felt that there was a significant risk of a sharp FALL in long and short term rates, e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- if it were felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.

External v. internal borrowing

- 6.4. The next financial year is expected to be one of historically abnormally low Bank Rates. This provides a continuation of the opportunity to review the strategy of undertaking new external borrowing against the use of internal borrowing
- 6.5. As long term borrowing rates are expected to be higher than rates on the loss of investment income and look likely to be so for the next couple of years the Council may prefer to avoid all new external borrowing in the next financial year in order to maximise savings in the short term. The running down of investments also has benefits of reducing exposure to interest rate and credit risk.
- 6.6. However, short term savings by avoiding new long term external borrowing in 2010/11 will also be weighed against the potential for incurring long term extra costs by delaying unavoidable new external borrowing until later years when long term rates are forecast to be significantly higher.
- 6.7. Against this background caution will be adopted with the 2010/11 treasury operations. The Director of Finance will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to the appropriate decision making body at the next available opportunity.

7. POLICY ON BORROWING IN ADVANCE OF NEED

- 7.1. The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be considered

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carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

7.2. In determining whether borrowing will be undertaken in advance of need the Council will;

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need
- ensure the ongoing 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 merits and demerits of alternative forms of funding
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.

8. DEBT RESCHEDULING

8.1. The introduction of the new PWLB rates structure on 1 November 2007 introduced a spread between the rates applied to new borrowing and repayment of debt and has meant that PWLB to PWLB debt restructuring is now much less attractive than before that date. However, significant interest savings may still be achievable through using LOBOs (Lenders Option Borrowers Option) loans and other market loans in rescheduling exercises.

8.2. As short term borrowing rates will be considerably cheaper than longer term rates, there are likely to be significant opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of their short term nature and the likely cost of refinancing those short term loans, once they mature, compared to the current rates of longer term debt in the existing debt portfolio. Any such rescheduling and repayment of debt is likely to cause a flattening of the Councils maturity profile as in recent years there has been a skew towards longer dated PWLB.

8.3. Consideration will also be given to the potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

8.4. The reasons for any rescheduling to take place will include:

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- the generation of cash savings and / or discounted cash flow savings
- enhance the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

8.5. All rescheduling will be reported to the Cabinet at the meeting following its action.

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APPENDIX 7 – Prudential Indicators**

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Prudential indicators	2009/10	2010/11	2011/12	2012/13
	out-turn	estimate	estimate	estimate
	£'000	£'000	£'000	£'000
Capital Expenditure				
Authorised' Non - HRA	76,872	54,627	6,590	9,288
Estimated Additional Expenditure		12,000	12,000	12,000
HRA (applies only to housing authorities)	8,730	10,094	10,000	10,000
TOTAL	85,602	76,721	28,590	31,288
Ratio of financing costs to net revenue stream				
Non - HRA	1.52%	3.93%	7.18%	8.99%
HRA (applies only to housing authorities)	12.98%	12.94%	12.29%	12.29%
Net borrowing				
brought forward 1 April	85,475	103,049	151,930	167,209
carried forward 31 March	103,049	151,930	167,209	183,395
I year borrowing requirement	17,574	48,881	15,280	16,186
In year Capital Financing Requirement				
Non - HRA	42,690	38,069	6,590	9,288
Estimated Additional Expenditure		12,000	12,000	12,000
HRA (applies only to housing authorities)	0	500	500	500
Less MRP	934	1,688	3,810	5,602
TOTAL	41,756	48,881	15,280	16,186
Capital Financing Requirement as at 31 March				
Non - HRA	103,375	156,499	175,089	196,377
HRA (applies only to housing authorities)	11,915	13,665	14,165	14,665
Less MRP (cum)		2,727	6,538	12,140
TOTAL	115,290	167,437	182,716	198,902
Incremental impact of capital investment decisions				
Increase in Council Tax (band D) per annum *	£0.00	£11.64	£37.32	£62.84

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Treasury management indicators	2009/10	2010/11	2011/12	2011/12
	out-turn	estimate	estimate	estimate
	£'000	£'000	£'000	£'000
Authorised Limit for external debt - borrowing	171,500	177,881	193,160	209,346
other long term liabilities	5,000	7,500	7,500	7,500
TOTAL	176,500	185,381	200,660	216,846
Operational Boundary for external debt - borrowing	145,500	197,881	213,160	229,346
other long term liabilities	5,000	7,500	7,500	7,500
TOTAL	150,500	205,381	220,660	236,846
Actual external debt	103,049	167,881	183,160	199,346
Upper limit for fixed interest rate exposure (% of Portfolio)	100%	100%	100%	100%
Upper limit for variable rate exposure (% of Portfolio)	30%	30%	30%	30%
Upper limit for total principal sums invested for over 364 days (per maturity date)	0	0	0	0

NB: The introduction of International Financial Reporting Standards (IFRS) in 2009/10 means that PFI liabilities will be brought on balance sheet when the 2009/10 final accounts are completed, this may affect one or more of the prudential indicators stated above which will be revised accordingly

Maturity structure of new fixed rate borrowing during 2010/11	upper limit	lower limit
under 12 months	15%	0%
12 months and within 24 months	30%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%
10 years and above	65%	0%

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The Council's Prudential Indicators for Capital Expenditure, External Debt and Treasury Management 2010/11

the CIPFA requirements of the Code are set out in bold italics

Capital Expenditure and Capital Commitments Prudential Indicators

The local authority will make reasonable estimates of the total capital expenditure that it plans to incur during the forthcoming financial year and at least the following two financial years. (The code goes on to require separate indicators for Housing Revenue Account (HRA) and non-HRA elements).

Prudential Indicators of Affordability - Ratio Affordability Measure

The local authority will estimate for the forthcoming financial year and (at least) the following two financial years the ratio of financing costs to net revenue stream. (The code goes on to require separate indicators for Housing Revenue Account (HRA) and non-HRA elements)

Prudential Indicators of Affordability - Incremental Council Tax Affordability Measures

The local authority will:

- I. forecast the total budgetary requirements for the authority based on no changes to the existing capital programme***
- II. forecast the total budgetary requirements for the authority with the changes to the capital programme included in the calculation***
- III. take the difference between (i) and (ii) and calculate the addition or reduction to Council tax that would result.***

This indicator is intended to show the effect of approving more capital expenditure on the Council Tax (i.e. the revenue effects of capital spending). The indicator relates to “*new capital investment decisions*”

Prudential Indicators of Affordability - Incremental Housing Rent Affordability Measures

A local authority that has a Housing Revenue Account will...

- I. forecast the total HRA budgetary requirements for the authority based on no changes to the existing capital programme***
- II. forecast the total HRA budgetary requirements for the authority with the changes to the capital programme included in the calculation***

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III. take the difference between (iv) and (v) and calculate the addition or reduction to weekly housing rents that would result.

Estimates of Capital Financing Requirement (CFR)

The local authority will make reasonable estimates of the total capital financing requirement at the end of the forthcoming financial year and the following two years. A local authority that has an HRA will identify separately estimates of the HRA and non HRA Capital Financing Requirement

The Capital Financing Requirement can simply be understood as the Council's underlying need to borrow money long term.

External Debt Prudential Indicators

The local authority will set for the forthcoming financial year and the following two financial years a prudential limit for its total external debt, gross of investments, separately identifying borrowing from other long term liabilities.

The Authorised Limit for Borrowing

The maximum amount the Council may borrow at any point in time in the year. It has to be set at a level the Council considers is "prudent". The authorised limit must be set so as to avoid circumstances in which the Council would need to borrow more money than this limit. Other long-term liabilities include items that would appear on the balance sheet of the Council that are similar but not identical to borrowing (e.g. the capital cost of lease arrangements).

Operational Boundary

The local authority will also set for the forthcoming financial year and the following two years an Operational Boundary for its total external debt, gross of investments, separately identifying borrowing from other long-term liabilities.

The operational boundary is a measure of the maximum borrowing the Council would normally have at any time during the year. The Code recognises that circumstances might arise when the boundary might be exceeded temporarily, but suggests that a sustained or regular pattern of borrowing above this level ought to be investigated, as a potential symptom of a more serious financial problem.

Treasury Management Prudential Indicators

The Prudential Code states that "in all cases, the process of setting prudential indicators for treasury management should be accompanied by a clear and

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integrated forward Treasury Management Strategy, and a recognition of the pre-existing structure of the authority's borrowing and investment portfolios."

The indicators that follow have been prepared taking account of the Treasury Management Strategy that forms part of the Council's Medium Term Resourcing Plan.

The first prudential indicator in respect of Treasury Management is that the local authority has adopted the CIPFA Code.

Swindon Borough Council adopted the *CIPFA Code of Practice for Treasury Management in the Public Services* at the meeting of Cabinet held on 10th April 2002. Treasury Management Practices (TMPs) have been established by the Director of Finance in line with the advice of Sector Treasury Services (the Council's retained advisers), and are kept up to date.

The first prudential indicator is therefore met.

Interest Rate Exposure

The local authority will set, for the forthcoming year and the following two years (at least), limits to its exposures to the effects of changes in interest rates. These prudential indicators will relate to both fixed interest rates and variable interest rates.

Prudential limits for the maturity structure of borrowing

The local authority will set for the forthcoming year both upper and lower limits with respect to the maturity structure of its borrowing

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APPENDIX 8 – ANNUAL INVESTMENT STRATEGY 2010/11

1. Investment Policy

1.1. The Council will have regard to the CLG's Guidance on Local Government Investments ("the Guidance") issued in March 2004, any revisions to that guidance, the Audit Commission's report on Icelandic investments and the 2009 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's overall investment priorities are: -

- (a) the security of capital and
- (b) the liquidity of its investments.

1.2. The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity.

1.3. The borrowing of monies purely to invest or on-lend and make a return is unlawful and this Council will not engage in such activity.

1.4. All investments with the UK Government, or a UK local authority or parish, in addition to other bodies with a high credit rating, may be classified as either specified or non-specified investments. The main difference between the two categories is that specified investments have a maturity period of less than one year. All investments, whether managed in-house or by external fund managers, may be either specified or non-specified investments. The main use of non-specified investments will be by the external fund managers, who are mandated to deal in UK gilts with a maturity period of more than one year. It is recommended that Swindon Borough Council do not place any non-specified investments in the current climate.

1.5. It is standard practice that Council investments, other than those with the UK Government or a local authority, will only be made with those bodies that have the very highest credit rating. For money market funds this will mean a AAA credit rating, for banks and building societies this will mean a short term rating of F1+ according to the Fitch Ratings Ltd, which is one of the authorised credit rating agencies as stated in the legislation. The Council receives credit rating updates daily, which helps to ensure that new investments are made with bodies that have the highest credit rating.

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- 1.6. The in-house investment strategy provides for funds to the value of £20 million to be made available for immediate dis-investment if necessary, which is sufficient to cover the regular monthly payments. Funds surplus to the monthly requirement will be invested for longer periods in order to take advantage of higher investment rates. Interest rates will be monitored in conjunction with the Council's external treasury advisers, with the possibility of entering into forward deals, where the terms of the investment are agreed up to one year in advance of the start date. Longer-term investments, may also be considered, with the authorisation of the Director of Finance
- 1.7. The Council's external fund manager, Investec, will comply with the Annual Investment Strategy. The agreement between the Council and the fund manager additionally stipulate guidelines and duration and other limits in order to contain and control risk.
- 1.8. The Council, in conjunction with its treasury advisor Sector, will use Fitch, Moodys and Standard and Poors ratings to derive its credit criteria, as well as the use of other data. All credit ratings will be monitored and acted upon daily. The Council is alerted to changes to ratings of all three agencies through its use of the Sector creditworthiness service.
- 1.9. 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 body is placed on negative rating watch (i.e. there is a reasonable probability of a rating change in the short term and the likelihood of that change being negative) and it is currently near the floor of the of the minimum acceptable rating for placing investments with that body, then no further investments will be made with that body.

2. Creditworthiness policy

- 2.1. The Council utilises the creditworthiness service provided by Sector Treasury Services. This service has been progressively enhanced over the last year and now uses a sophisticated modelling approach with credit ratings from all three rating agencies - Fitch, Moodys and Standard and Poors, forming the core element. However, it does not rely solely on the current credit ratings of counterparties but also uses the following as overlays : -

- credit watches and credit outlooks from credit rating agencies

Further information on the subject of this report can be obtained from Paul Smith on *Direct Dial No. 01793 463976* or Email psmith2@swindon.gov.uk.

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- Credit Default Swap (CDS) spreads (an indicator of risk) to give early warning of likely changes in credit ratings
- sovereign ratings to select counterparties from only the most creditworthy countries

2.2. This modelling approach combines credit ratings, credit watches, credit outlooks and CDS spreads in a weighted scoring system for which the end product is a series of colour code bands which indicate the relative creditworthiness of counterparties. These colour codes are also used by Sector to determine the recommended duration for investments that are place with individual counterparties

2.3. Sector recommend the following for banks which are rated in each colour coded band:

- Purple Lend to for up to 2 years
- Blue Lend to for up to 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange Lend to for up to 1 year
- Red Lend to for up to 6 months
- Green Lend to for up to 3 months
- No Colour Not to be used.

2.4. The Council utilises these recommendations in making its investment decisions but in order to further ensure the security of taxpayers funds, will not lend to any counterparty for more than 1 year and will not lend to any counterparty in the green colour coded band (as being below the overall credit rating required by Swindon Borough Council)

3. Country limits

3.1. 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)

4. Investment Strategy

4.1. Investment of in-house funds will be made with reference to the cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

4.2. Bank Rate has been unchanged at 0.50% since March 2009. Bank Rate is forecast to commence rising in quarter 3 of 2010 and then to rise steadily from thereon.

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4.3. The Council will avoid locking into longer term deals while investment rates are down at historically low levels unless exceptionally attractive rates are available which make longer term deals worthwhile.

4.4. At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

5. External fund managers

5.1. £36.8m (as at December 2009) of the Council's funds are externally managed on a discretionary basis by Investec

5.2. The Council's external fund manager will comply with the Annual Investment Strategy. The agreement between the Council and the fund manager additionally stipulate guidelines and duration and other limits in order to contain and control risk.

5.3. The fund manager's view on interest rates and opportunities for gilts/bonds is as follows: 'Gilt yields have started to rise, 10yr gilts are testing this year's high of c.4%. We expect shorter dated gilts to rise next year as Quantitative Easing draws to a close and the first rise in official rates moves closer. The fund is well positioned to take advantage next year in Gilts and longer dated CD's at yields significantly above current rates.'

5.4. The external fund managers projection of the performance of the fund in 2010/11 is :

Best: 2.75%

Central 2.00%

Lower: 1.25%

6. Policy on the use of external service providers

6.1. The Council uses Sector Treasury Services as its external treasury management advisers.

6.2. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

6.3. It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

7. Scheme of delegation

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7.1. The 2004 Investment guidance requires that the Annual Investment Strategy should include information around the Scheme of Delegation and the Role of the section 151 officer. These are included as Appendices 7 and 9.

8. Loans to 3rd Parties

8.1. The Council's normal attitude to lending is very risk averse. Wider powers to invest in third parties do, however, exist in the Local Government Act 2003 (Chapter 26 Section 12), which defines the power to invest as:

- (a) for any purpose relevant to its functions under any enactment
- (b) for the prudent management of its financial affairs.

8.2. In order to pursue its regeneration and wider strategic objectives, the Council may enter into a series of joint venture arrangements with private sector partners. There may be circumstances in which it is advantageous in financial and risk terms for the Council to consider acting as banker for a scheme, subject to the terms and exposure being acceptable. In this context, Council has approved that the annual investment strategy permits the Directors of Finance and Law and Democratic Services, in consultation with the Cabinet Member for Finance and Benefits, to invest in such schemes provided that the overall terms of the arrangement are suitably advantageous for the Council, subject to the Soft Loan accounting requirements.

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APPENDIX 9 Annual Minimum Revenue Provision Report

MRP Policy Statement

The Council implemented the new Minimum Revenue Provision (MRP) guidance in 2008/09, and will assess its MRP for 2010/11 in accordance with the main recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act 2003.

The major proportion of the MRP for 2010/11 will relate to the more historic debt liability that will continue to be charged at the rate of 4%, in accordance with option 1 of the guidance. Certain expenditure reflected within the debt liability at 31st March 2010 will under delegated powers be subject to MRP under option 3 which will be charged over a period which is reasonably commensurate with the estimated useful life applicable to the nature of expenditure, using the equal annual instalment method. For example, capital expenditure on a new building, or on the refurbishment or enhancement of a building, will be related to the estimated life of that building.

Estimated life periods will be determined under delegated powers. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Council. ***However, the Council reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate, such as for complex infrastructure projects as per paragraph 13 of the guidance notes.***

As some types of capital expenditure incurred by the Council are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

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