APPENDIX 1

TREASURY MANAGEMENT STRATEGY 2014-15

Cyngor Bwrdeistref Sirol
Pen-y-bont ar Ogwr
BRIDGEND
County Borough Council

1.0 Introduction

The Council adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services*: *Code of Practice 2011 Edition* (the CIPFA Code) in February 2012 which requires the Council to approve a treasury management strategy before the start of each financial year.

In addition to the Code of Practice, the Welsh Government (WG) issued revised *Guidance on Local Authority Investments* in April 2010 that requires the Council to approve an Investment Strategy before the start of each financial year.

This Strategy fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to both the CIPFA Code and the WG Guidance.

The Council has an integrated Treasury Management Strategy where borrowing and investments are managed in accordance with best professional practice. The Council borrows money either to meet short term cash flow needs or to fund capital schemes approved within the capital programme. Therefore any actual loans taken are not associated with particular items of expenditure or assets. The Council is exposed to financial risks including the potential loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

The Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Cabinet, and for the execution and administration of treasury management decisions to the Section 151 Officer, who will act in accordance with the organisation's strategy, Treasury Management Practices (TMP) and CIPFA's Standard of Professional Practice on Treasury Management. Council will receive reports on its treasury management activities, including as a minimum, an annual strategy in advance of the year, a mid-year review and an annual report after its financial year end. Quarterly reports will also be received by Cabinet.

The Council nominates the Audit Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

2.0 Economic Context and Forecasts for Interest Rates

Economic background: The Bank of England's Monetary Policy Committee (MPC) principal measure in its Forward Guidance on interest rates is the Labour Force Survey (LFS) unemployment rate of 7%. This is the threshold for when the MPC would generally consider whether or not to raise interest rates. The unemployment rate was 7.6% as at December 2013, but is not forecast to fall below the threshold until 2016, so the MPC is unlikely to raise the Bank Rate from its current level of 0.50% before this date.

Stronger growth data in 2013 (0.4% in Q1, 0.7% in Q2 and 0.8% in Q3) alongside an increase in property prices have led markets to price in an earlier rise in rates than warranted under Forward Guidance and the broader economic backdrop. However, with jobs growth picking up slowly, many employees working shorter hours and the impact of the Welfare Benefit Reform Bill, growth is likely to be gradual. The Council's Treasury Management Advisers (Arlingclose) forecasts that the MPC will maintain its resolve to keep interest rates low until the recovery is convincing and sustainable.

Credit outlook: The credit risk of banking failures has diminished, but not dissipated altogether. Regulatory changes are afoot in the UK, US and Europe to move away from the bank bail-outs of previous years to bank resolution regimes in which shareholders, bond holders and unsecured creditors are 'bailed in' to participate in any recovery process. This is already manifested in relation to holders of sub-ordinated debt issued by the Co-operative Bank which will suffer a cut on its conversion bail-in to alternative securities and/or equity. There are also proposals for EU regulatory reforms to Money Market Funds which will, in all probability, result in these funds moving to a VNAV (variable net asset value) basis and losing their 'triple-A' credit rating. Diversification of investments between creditworthy counterparties to mitigate bail-in risk will become even more important in the light of these developments.

Interest rate forecast: Arlingclose's forecast is for the Bank Rate to remain flat until late 2016. Gilt yields are expected to rise over the forecast period with medium- and long-dated gilts expected to rise by between 0.7% and 1.1%.

Arlingclose (Council's TM Advisers) central interest rate forecast – December 2013

	Bank Rate	3 Bank month LIBID	1 Year LIBID	20-year gilt yield*	50-year gilt yield*
Dec 2013	0.50	0.45	0.90	3.25	3.45
Mar 2014	0.50	0.45	0.95	3.30	3.50
June 2014	0.50	0.50	0.95	3.35	3.55
Sept 2014	0.50	0.55	0.95	3.40	3.60
Dec 2014	0.50	0.55	1.00	3.45	3.65
Mar 2015	0.50	0.55	1.05	3.50	3.70
June 2015	0.50	0.55	1.10	3.55	3.75
Sept 2015	0.50	0.60	1.15	3.65	3.80
Dec 2015	0.50	0.65	1.20	3.75	3.85
Mar 2016	0.50	0.70	1.25	3.85	3.95
June 2016	0.50	0.80	1.30	4.05	4.05
Sept 2016	0.50	0.80	1.40	4.15	4.15
Dec 2016	0.50	0.80	1.40	4.15	4.15

3.0 The Council's Current Treasury Management Position

The Council's debt and investment position as at 1 January 2014 is shown below:

		Principal £m	Average Rate %
Fixed rate long term funding	PWLB*	77.63	4.70
	Market	-	-
Variable rate long term funding	PWLB*	-	-
	Market LOBO**	19.25	4.65
Total External Borrowing***		**96.88**	**4.69**
Other Long Term Liabilities*** (including PFI)		22.06	
TOTAL DEBT		**118.94**	
Fixed rate investments		8.50	0.36
Variable rate investments		9.85	0.53
TOTAL INVESTMENTS****		**18.35**	**0.45**
NET DEBT		**100.59**	

* Public Works Loan Board (PWLB)

** Lender's Option Borrower's Option (LOBO)

*** Long term borrowing/liabilities include all instruments with an initial term of 365 days or more.

**** The investment totals include instant access deposit accounts which are included as "Cash" in the Council's balance sheet and also investments shown as "Cash Equivalents" in the Council's balance sheet that mature in 3 months or less from the date of acquisition and that are readily convertible to known amounts of cash with insignificant risk of change in value

Fixed rate in the above table includes instruments which are due to mature in the year

Details of the debt maturity profile are shown in **Schedule A**. The £19.25m showing as maturing in 2054, relates to Lender's Option Borrower's Option (LOBO) loans which may be re-scheduled in advance of this maturity date. The LOBO rate and term may vary in the future depending upon the prevailing market rates, the lender exercising their option to increase rates at one of the bi-annual trigger points and therefore, the Council being given the option to accept the increase or to repay the loan without incurring a penalty. The next trigger point is 22 July 2014 and although the Council understands that the lender is unlikely to exercise this option in the current low interest rate environment, an element of refinancing risk remains and the Council would take the option to repay these loans at no cost if it has the opportunity to do so.

Investments are anticipated to drop from £18.35m on 1 January 2014 to between £8m to £12m by the 31 March 2014. This is due partly to the reduction in income collected from Council Tax and National Non-Domestic Rates in February and March 2014 and expenditure expected for the capital programme.

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing. CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Forecast changes in these sums are included in the Treasury Management and Prudential Indicators shown in **Schedule B** which shows that the Council expects to comply with this recommendation during 2014-15 and the following three years.

4.0 <u>Borrowing Strategy</u>

The major **objectives** to be followed in 2014-15 are:-

- to minimise the revenue costs of debt,
- to manage the Council's debt maturity profile i.e. to leave no one future year with a high level of repayments that could cause problems in re-borrowing (the current debt maturity profile is shown in **Schedule A**),
- to effect funding in any one year at the cheapest cost commensurate with future risk,
- to forecast average future interest rates and borrow accordingly,
- to monitor and review the level of variable interest rate loans in order to take greater advantage of interest rate movement,
- to reschedule debt if appropriate, in order to take advantage of potential savings as interest rates change, and
- to maximise the use of all capital resources including borrowing, both supported and unsupported, useable capital receipts and grants and contributions.

The Section 151 Officer will take the most appropriate form of borrowing depending on the prevailing interest rates at the time and the expected borrowing requirement for 2014-15 is £5m at an estimated rate of 4.60%.

Given the significant cuts to public expenditure and in particular to local government funding, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. The uncertainty over future interest rates increases the risks associated with treasury activity. As a result the Council will take a cautious approach to its treasury strategy. With short-term interest rates currently much lower than long term rates, it is likely to be more cost effective in the short term to either borrow short term loans or use internal resources. Short term and variable rate loans expose the Council to the risk of short term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates as shown in the treasury management indicators in **Schedule B.**

However, with long term rates forecast to rise in the coming years, any such short term savings will need to be balanced against the potential longer-term costs. The Council's Treasury Management advisers will assist the Council with this 'cost of carry' and breakeven analysis.

The **approved sources** of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB)
- UK local authorities
- any institution approved for investments (see Investment Strategy)
- any other bank or building society authorised by the Prudential Regulation Authority to operate in the UK
- UK public and private sector pension funds (except the Council's Pension Fund)
- capital market bond investors
- special purpose companies created to enable joint local authority bond issues.

The Council has previously raised the majority of its long-term borrowing from the PWLB, but will also investigate other sources of finance, such as local authority loans and bank loans, that may be available at more favourable rates.

Before any long term borrowing is undertaken an assessment of the Council's borrowing requirement must be made. This will include:

- a calculation of the funds needed to meet capital expenditure,
- options appraisal to determine the funding decision, as required by the Prudential Code,
- ensuring that the level of long term borrowing is consistent with the Treasury Management Strategy and the Treasury Management and Prudential Indicators,
- assessment of the PWLB interest rates and current market rate to ascertain the cheapest source of finance, and
- the selection, dependent upon interest rate levels, of the most appropriate period for borrowing, bearing in mind the maturity profile of existing Council debt.

Debt Rescheduling: The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. The Council may take advantage of this and replace some higher rate loans with new loans at lower interest rates, or repay loans without replacement, where this is expected to lead to an overall saving or reduction in risk.

5.0 Investment Strategy

Both the CIPFA Code and the WG Guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, balancing the risk of incurring losses from defaults against receiving unsuitably low investment income.

The major **objectives** to be followed in 2014-15 are:-

- To maintain capital **security**;
- To maintain **liquidity** so funds are available when expenditure is needed;
- To achieve the **yield** on investments commensurate with the proper levels of security and liquidity.

Approved Instruments: The Council may lend or invest money using any of the following instruments:

- interest-bearing bank accounts,
- fixed term deposits and loans,
- callable deposits and loans where the Council may demand repayment at any time (with or without notice),
- callable deposits and loans where the borrower may repay before maturity,
- certificates of deposit,
- bonds, notes, bills, commercial paper and other marketable instruments, and
- shares in money market funds and other pooled funds.

Investments will be made after the following steps have been taken:

- assessment of the available funds and the suitability of the period over which the investment is to be made,
- reference to the list of approved counterparties and to the maximum limit on funds to be placed with a single organisation,
- the completion of adequate documentation to ensure the protection of the Council's interests,
- checks to ensure that the interest rates offered are comparable with the other available investments, and
- due regard has been paid to the fact that a comparatively high return will usually entail a higher level of risk.

With short term interest rates currently much lower than long-term rates, due consideration will also be given to using surplus funds to make early repayments of long term borrowing if appropriate.

Specified Investments: This is an investment which offers high security and high liquidity. It is a low risk investment where the possibility of loss of principal or investment income is negligible and satisfies the conditions below as defined by *WG Investment Guidance*:-

- denominated in sterling,
- contractually committed to be paid within 12 months of arrangement (364 days),
- not defined as capital expenditure by legislation, and
- invested with one of:
  - body or in an investment scheme of high credit quality (Council's definition detailed below),
  - the UK Government,
  - a UK local authority,
  - a UK parish or community council

The Council's definition of **"high credit quality"** is deemed to be counterparties having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. Overseas subsidiaries of foreign banking groups will normally be assessed according to the country of domicile of the parent organisation. However, Santander UK plc (a subsidiary of Spain's Banco Santander) and Clydesdale Bank plc (a subsidiary of National Australia Bank) will be classed as UK banks due to their substantial UK franchises and arms- length parent-subsidiary relationships.

Non-specified Investments: Any investment that does not fall into the criteria detailed above under the Specified definition. The Council does not intend to make any investments denominated in foreign currencies. Non-specified investments will therefore be limited to:

- long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement,
- those that are defined as capital expenditure by legislation, such as shares in money market funds and other pooled fund, and
- investments with bodies and schemes not meeting the definition on high credit quality above.

All investments longer than 364 days will be made with a cautious approach to cash flow requirements and will only be entered into with prior advice from the Council's Treasury Management Advisers.

The WG Guidance requires the Council's Investment Strategy to set an overall limit for non-specified investments which is currently set at £25m. The table below shows the non-specifed categories and the relevant limits – the total of the individual limits exceed £25m, however at any one point in time a maximum of £**25m** of investments could be in one of the following non-specified categories with the following category limits:

Non-Specified Investment Limits	**Category Total Cash limit**
Total long-term investments	£15m
Total money market funds and other pooled funds	£ 8m
Total building societies not meeting the Council's high credit quality definition (but with assets greater than £500m)	£ 6m
Total investments (excluding building societies – separate limit) not meeting the Council's high credit quality definition	£ 2m

The combined values of specified and non-specified investments with any one organisation are subject to the limits detailed above and the approved counterparties and limits shown in the table below. A group of banks under the same ownership will be treated as a single organisation for limit purposes.

The Council's investments have historically been placed in bank and building society deposits and local and central government, however, investments may be made with any public or private sector organisations that meet the above credit criteria. This reflects a lower likelihood that the UK and other governments will support failing banks as the bail-in provisions in the *Banking Reform Act 2014* and the EU *Bank Recovery and Resolution Directive* are implemented.

The Council's **approved counterparties** are shown in the table below:

Counterparty	Credit Rating (or equivalent)	Time Limit	Cash Limit
UK registered banks, building societies and other organisations and securities whose lowest published long-term credit rating from Fitch, Moody's and Standard & Poor's is:	AAA AA+ AA AA-	6 years 5years 4years 3years	£8m each of which no more than £3m over 1 year
	A+ A A-	2 years 1 year 1 year 6 months	£6m of which no more than £3m over 1 year £5m £3m £5m (higher cash limit than 1 year due to shorter duration and less perceived risk)
UK Central Government	n/a	10 years	Unlimited
UK Local Authorities** but excluding parish and community councils	n/a	10 years	£15m
The Council's current account bank if it fails to meet the above criteria*		next day	£3m
UK registered building societies whose lowest published long-term credit rating from Fitch, Moody's and Standard & Poor's is:	BBB	100 days	£2m
UK registered building societies without credit ratings with assets greater than £500m		100 days	£1m
Banks owned and domiciled in foreign countries with a sovereign rating of AA+ or higher	A+	6 months	£3m
Money market funds** and other pooled funds*		n/a	£2m
Any other organisation and pooled fund subject to an external credit assessment and specific advice from the Council's treasury management advisers		1 year 6 months	£1m £2m

**following discussion and approval from Treasury management advisers*
*** as defined in the Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003*
****as defined in the Local Government Act 2003, and similar authorities in Scotland*

N.B. Long-term credit ratings refers to those published from Fitch, Moody's and Standard and Poor

Some of the counterparties in the above table are explained in more detail below:

Current Account Bank: A competitive tender exercise was held in 2012 and the Council's current accounts are held with the Co-operative Bank which is currently rated below the minimum credit rating shown in the above counterparty table. The Council operates a pooling system on all accounts and the balance is kept as close to zero as possible and does not currently place any investments with them. However, should their credit rating improve the Council would consider reviewing this providing that investments can be withdrawn on the next working day, and that the bank maintains a credit rating no lower than BBB- (the lowest investment grade rating). A bank retendering exercise is expected to be undertaken in 2014 with a view to awarding a new banking contract in the latter part of 2014-15 as the Co-Operative Bank announced in November 2013 that it does not wish to support local government banking beyond 2015-16, although it will honour existing contracts.

Building Societies: are mutually owned financial institutions with a more cautious business model than shareholder owned banks. They are tightly regulated by the Prudential Regulation Authority, which detects problems at an early stage. The probability of a building society defaulting on its financial obligations is therefore low. The Council takes additional comfort from the building societies' regulatory framework and insolvency regime where, in the unlikely event of a building society liquidation, the Council's deposits would be paid out in preference to retail depositors. The Council would therefore consider investing with unrated building societies where independent credit analysis shows them to be suitably creditworthy. The Government has announced plans to amend the building society insolvency regime alongside its plans for wide ranging banking reform, and investments in lower rated and unrated building societies will therefore be kept under continuous review.

Money Market Funds: These funds are pooled investment vehicles consisting of money market deposits and similar instruments. They have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager. A credit rating is not shown in the counterparty table above as there are EU proposals to stop money market funds from having credit ratings. To date the Council has not used money market funds.

Other Pooled Funds: The Council may consider using pooled bond, equity and property funds that offer enhanced returns over the longer term, but are potentially more volatile in the shorter term. To date the Council has not used any pooled funds but if it did their performance and continued suitability in meeting the Council's investment objectives would be monitored regularly.

Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes in ratings as they occur. They use long-term credit ratings from the three main rating agencies Fitch Ratings Ltd., Moody's Investors Service and Standard & Poor's Financial Services to assess the risk of investment default. The lowest available counterparty credit rating will be used to determine credit quality, unless an investment specific rating is available.

Credit Rating Criteria and their Use: Long-term ratings are expressed on a scale from AAA (the highest quality) through to D (indicating default). Ratings of BBB- and above are described as investment grade, while ratings of BB+ and below are described as speculative grade. The Council's credit rating criteria are set to ensure that it is very unlikely the Council will hold speculative grade investments, despite the possibility of repeated downgrades.

Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

Where a credit rating agency announces that a rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Other Information on the Security of Investments: The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

When deteriorating financial market conditions affect the creditworthiness of all organisations this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Council's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

Investment Balances: The Council holds surplus funds representing income received in advance of expenditure plus balances and reserves held. Based on its cash flow forecasts, the Council anticipates its fund balances in 2014-15 to range from £5m to £40m. The actual balance varies because of the cash flow during the month and year as to when income is received (such as specific grant income, housing benefits subsidy and Revenue Support Grant) and payments are made (such as salaries and wages, major capital expenditure and loan repayments).

6.0 Treasury Management and Prudential Indicators

The 2011 Treasury Management Code and Prudential Code require the Council to set and report on a number of Treasury Management and Prudential Indicators. **Schedule B** revises some of the indicators for 2013-14, 2014-15, 2015-16, 2016-17 and introduces new indicators for 2017-18 to be consistent with the principles contained in the Medium Term Financial Strategy. The indicators either summarise the expected activity or introduce limits upon the activity, and reflect the underlying capital programme.

7.0 Annual Minimum Revenue Provision Statement 2014-15

Where a Council finances capital expenditure by debt, it must put aside revenue resources to repay that debt in later years. This amount charged to revenue is called the Minimum Revenue Provision (MRP). Under the Local Authority (Capital Finance and Accounting) (Amendment) (Wales) Regulations 2008, an Annual Minimum Revenue Provision (MRP) Statement needs to be produced that details the methodology for the MRP charge. There is not a statutory minimum for the amount set aside. It needs to be considered a prudent provision to ensure that the debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits or in the case of borrowing supported by Welsh Government's Revenue Support Grant reasonably commensurate with the period implicit in the determination of that grant. This is detailed in **Schedule C.**

The methodology for charging MRP has been revised for 2014-15 and future years as a result of a complete review of the capital financing budget. This has resulted in revenue savings within the Medium Term Financing Strategy of £250k 2014-15, £250k 2015-16 and £200k in 2016-17.

8.0 Performance Indicators

The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators as opposed to the treasury management and prudential indicators which are predominantly forward looking. One debt performance indicator is where the average portfolio rate of interest is compared to an appropriate average available such as the average PWLB Debt for Welsh and UK Local Authorities. The rate of return on investments is monitored against the benchmark of the average 7 day London Inter Bank rate (LIBID rate) and will also be benchmarked against the average Bank Rate.

9.0 Other Items

The Council is required by CIPFA or WG to include the following additional items:

Policy on Use of Financial Derivatives: The Localism Act 2011 includes a general power competence that removes the uncertain legal position over English local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment). These instruments are used by organisations to manage exposure to interest rate or exchange rate fluctuations. Although this change does not apply to Wales, the latest CIPFA Code requires authorities to clearly state their policy on the use of derivatives in the annual strategy .In the absence of any legislative power, the Council's policy is not to enter into standalone financial derivatives transactions such as swaps, forwards, futures and options. Embedded derivatives within loans and investments (including interest rate collars and forward deals) may be used and the risks they present will be managed in line with the overall treasury risk management strategy.

Investment Advisers: The Council has appointed Arlingclose Limited as treasury management advisers to provide advice and information relating to its borrowing and investment activities,. The quality of this service is controlled by having regular meetings with the advisers and regularly reviewing the service provided.

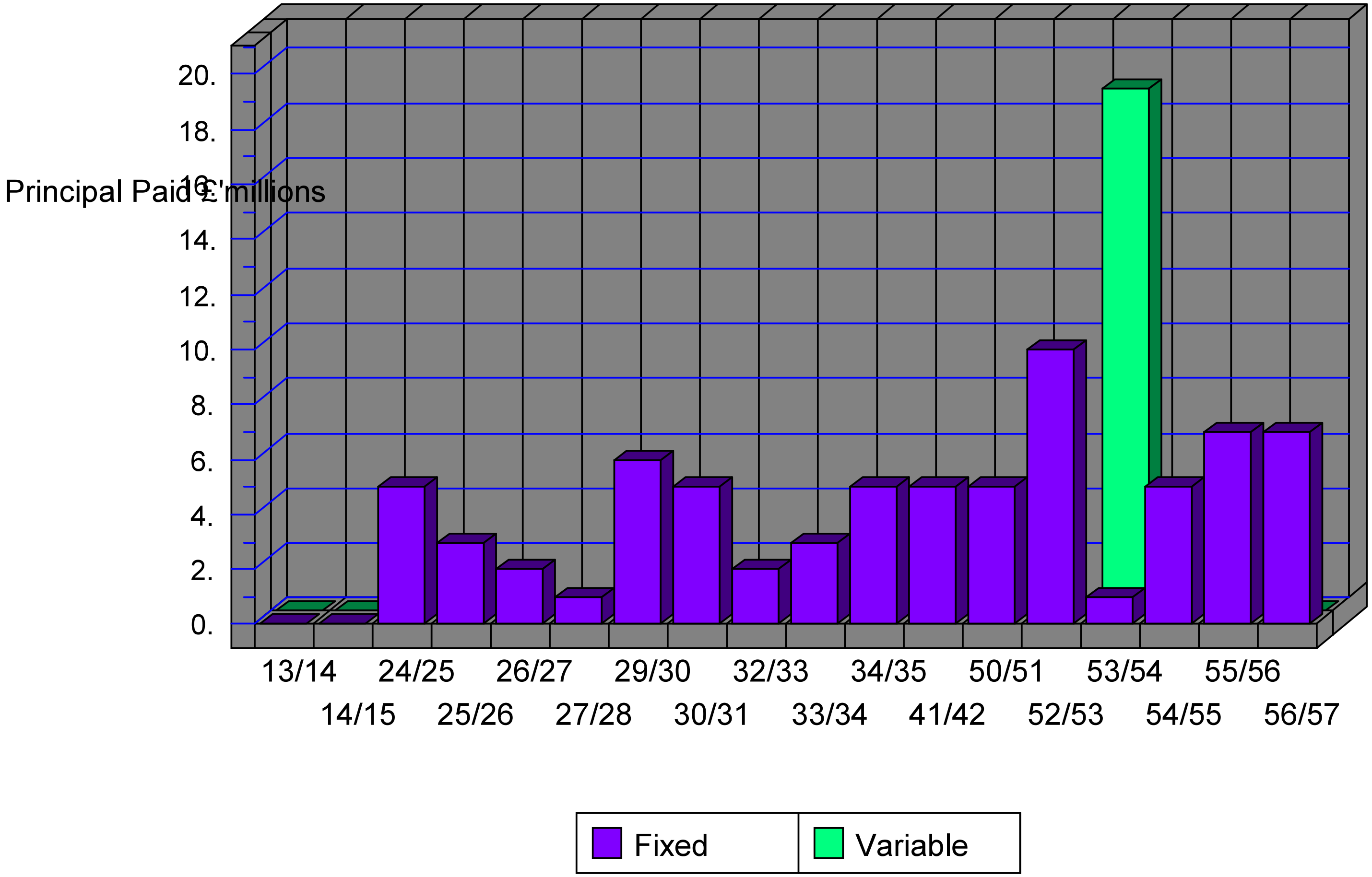
Investment of Money Borrowed in Advance of Need: The Welsh Government maintains that the borrowing of monies purely to invest or on-lend and make a return is unlawful and this Council will not engage in such activity. This Council's borrowing is not linked to the financing of specific items of expenditure. The Council's Capital Financing Requirement (CFR) as at 1 January 2014, was in excess of the actual debt of the Authority. This indicates that there was no borrowing in advance of need.

Investment Training: The Treasury Management Team receives training from the Council's Treasury Management advisers. The Council also supports personal development so individuals enhance their own knowledge through reading CIPFA guidance, publications and research on the internet.

Schedule A

Long Term Debt Outstanding – Principal due to be paid

MATURITY ANALYSIS - 2014 to 2057



Schedule B

TREASURY MANAGEMENT INDICATORS

The following indicators (which are forward looking parameters) form part of the CIPFA Code of Practice on Treasury Management. They enable the Council to measure and manage its exposure to Treasury Management risks using the following indicators.

The Council needs to set the upper limits to its **Interest Rate Exposure** for the effects of changes in interest rates. There are two treasury management indicators that relate to both fixed interest rates and variable interest rates. These limits have been calculated with reference to the net outstanding principal sums and are set to control the Council's exposure to interest rate risk.

No.	Interest Rate Exposure	2014-15 Est. £m	2015-16 Est. £m	2016-17 Est. £m	2017-18 Est. £m
	Total Projected Principal Outstanding on Borrowing 31 March	101.87	106.87	111.87	116.87
	Total Projected Principal Outstanding on Investments 31 March	9.00	8.00	7.00	6.00
	Net Debt Outstanding	**92.87**	**98.87**	**104.87**	**110.87**
1.	**Upper Limit on fixed interest rates (net debt) exposure**	130.00	135.00	140.00	145.00
2.	**Upper Limit on variable interest rates (net debt) exposure**	50.00	52.00	55.00	55.00

The Section 151 Officer will manage interest rate exposures between these limits in 2014-15.

A further indicator for Treasury Management measures the **Maturity Structure of Borrowing** and is the amount of projected borrowing that is fixed rate, maturing in each period as a percentage of total projected fixed rate borrowing. This indicator is set to control the Council's exposure to refinancing risk and has been set to allow for the possible restructuring of long term debt where this is expected to lead to an overall saving or reduction in risk.

No	Maturity structure of fixed rate borrowing during 2014-15	Upper limit	lower limit
3.	Under 12 months	50%	0%
	12 months and within 24 months	25%	0%
	24 months and within 5 years	50%	0%
	5 years and within 10 years	60%	0%
	10 years and above	100%	40%

The Upper Limit for **Total Principal Sums Invested over 364 days** controls the amount of longer term investments which mature beyond the period end. This is set to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments.

No.		2014-15 £m	2015-16 £m	2016-17 £m	2017-18 £m
4.	**Upper Limit - Total Principal Sum Invested more than 364 day days**	12	10	9	8

2.0 PRUDENTIAL INDICATORS

The Prudential Indicators are required to be set and approved by Council in accordance with CIPFA's *Prudential Code for Capital Finance in Local Authorities.*

Council is required to formally adopt CIPFA's Treasury Management Code and the revised version of the 2011 code was adopted by Council on 22 February 2012.

Prudential Indicators for Prudence

The following Prudential Indicators are based on the Council's capital programme which is subject to change.

The Council's capital expenditure plans are summarised below and this forms the first prudential indicator for Prudence. The total capital expenditure is funded from capital grants and contributions, capital receipts and revenue with the remainder being the **Net Financing Need for the Financial Year** to be met from borrowing.

No.	Prudential indicators For Prudence	2013-14 £'000 Proj.	2014-15 £'000 Est.	2015-16 £'000 Est.	2016-17 £'000 Est.	2017-18 £'000 Est.
1	**Estimates of Capital Expenditure**					
	Non – HRA	41,223	32,060	15,652	19,630	11,740
	Total Capital Expenditure	**41,223**	**32,060**	**15,652**	**19,630**	**11,740**
	Financed by :-					
	Capital Grants and Contributions	14,935	11,393	8,418	11,785	5,082
	Capital Receipts	6,245	12,005	2,002	3,913	2,726
	Revenue	820	0	0	0	0
	Net Financing Need for Year	**19,223**	**8,662**	**5,232**	**3,932**	**3,932**

The second Prudential Indicator is the **Capital Financing Requirement (CFR)** for the Council. This shows the total outstanding capital expenditure that has not been funded from either revenue or other capital resources. It is derived from the actual Balance Sheet of the Council. It is essentially a measure of the underlying need to finance capital expenditure and forms the basis of the charge to the General Fund under the Prudential Code system.

The process for charging the capital expenditure to revenue is a statutory requirement and is called the Minimum Revenue Provision (MRP).The actual MRP charge needs to be prudent – as detailed in the Council's MRP policy in **Schedule C.**

No.	Prudential indicators For Prudence	2013-14 £'000 Proj.	2014-15 £'000 Est.	2015-16 £'000 Est.	2016-17 £'000 Est.	2017-18 £'000 Est.
2	**Capital Financing Requirement (CFR)**					
	Opening CFR (1 April) excluding PFI	144,279	157,092	158,870	157,399	154,912
	Opening PFI CFR	20,218	19,776	19,300	18,787	18,235
	Opening Finance Lease CFR	95	41	0	0	0
	Opening Innovation Centre	845	816	769	719	663
	Opening HALO	144	1,267	1,150	1,033	917
	Total Opening CFR	**165,581**	**178,992**	**180,089**	**177,938**	**174,727**
	Movement in CFR excluding PFI & other liab	12,812	1,778	(1,471)	(2,487)	(2,150)
	Movement in PFI CFR	(442)	(476)	(512)	(552)	(595)
	Movement in Finance Lease CFR	(54)	(41)	0	0	0
	Movement in Innovation Centre CFR	(28)	(47)	(51)	(55)	(60)
	Movement in HALO CFR	1,123	(117)	(117)	(117)	(117)
	Total Movement in CFR	**13,411**	**1,097**	**(2,151)**	**(3,211)**	**(2,922)**
	Closing CFR (31 March)	**178,992**	**180,089**	**177,938**	**174,727**	**171,805**
	Movement in CFR represented by :-					
	Net Financing Need for Year (above)	19,223	8,662	5,232	3,932	3,932
	Adjustment for Halo	1,239	-	-	-	-
	Minimum and Voluntary Revenue Provisions*	(7,051)	(7,565)	(7,383)	(7,143)	(6,854)
	Total Movement	**13,411**	**1,097**	**(2,151)**	**(3,211)**	**(2,922)**

*Minimum Revenue Provision (MRP) and Voluntary Revenue Provision (VRP) represent the revenue charge for the repayment of debt and includes MRP for the Public Finance Initiative (PFI), Finance Leases, Innovation Centre and HALO

Limits to Borrowing Activity

The Council's long term borrowing at the 31 December 2013 was £96.88m as detailed in section 3 of the Strategy. External Borrowing can arise as a result of both capital and revenue expenditure and timing of cash flows. Because the Council has an integrated Treasury Management Strategy there is no association between individual loans and particular types of expenditure. Therefore, the Capital Financing Requirement and actual external borrowing can be very different.

The **Gross Debt** position (Borrowing and Long Term Liabilities) is shown below:

No.	Prudential indicators For Prudence Gross Debt 31 March	2013-14 £'000 Proj.	2014-15 £'000 Est.	2015-16 £'000 Est.	2016-17 £'000 Est.	2017-18 £'000 Est.
3	External Borrowing	96,883	101,867	106,867	111,867	116,867
	Long Term Liabilities (including PFI)	21,900	21,219	20,539	19,815	19,043
	Total Gross Debt	**118,783**	**123,086**	**127,406**	**131,682**	**135,910**

Within the Prudential Indicators, there are a number of key indicators to ensure the Council operates its activities within well-defined limits. One key control is to ensure that over the medium term, debt will only be for a capital purpose. The Council needs to ensure that external debt does not, except in the short term, exceed the Capital Financing Requirement for 2013-14 (i.e. the preceding year) plus the estimates of any additional capital financing requirement for the current and next three financial years, however 2017-18 has also been included to be consistent with the Medium Term Financial Strategy.

No.	Prudential indicators For Prudence	2013-14 £'000 Proj.	2014-15 £'000 Est.	2015-16 £'000 Est.	2016-17 £'000 Est.	2017-18 £'000 Est.
4	**Gross Debt & the CFR**					
	Total Gross Debt	118,783	123,086	127,406	131,682	135,910
	Closing CFR (31 March)	**178,992**	**180,089**	**177,938**	**174,727**	**171,805**

As can be seen from the above table, the Council does not have any difficulty meeting this requirement in 2013-14 and does not envisage any difficulties in the current and future years. This view takes into account current commitments, existing plans and the proposals for next year's budget.

A further two Prudential Indicators control the Council's overall level of debt to support Capital Expenditure. These are detailed below:-

- The **Authorised Limit** for External Debt – this represents the limit beyond which borrowing is prohibited. It reflects a level of borrowing that could not be sustained even though it would be affordable in the short term. It needs to be set and approved by Members.

- The **Operational Boundary** for External Debt – this is not an actual limit and actual borrowing could vary around this boundary during the year. It is based on the probable external debt during the course of the year.

No.	Prudential indicators For Prudence	2013-14 £m	2014-15 Est. £m	2015-16 Est. £m	2016-17 Est. £m	2017-18 Est. £m
5	**Authorised limit for external debt**					
	Borrowing	146	140	145	150	155
	Other long term liabilities	30	30	30	30	30
	Total	**176**	**170**	**175**	**180**	**185**
6	**Operational Boundary**					
	Borrowing	115	115	120	125	130
	Other long term liabilities	24	25	25	25	25
	Total	**139**	**140**	**145**	**150**	**155**

<u>Prudential Indicators for Affordability</u>

The Prudential Code Indicators Numbered 1 to 6 above cover the overall controls on borrowing and financing of capital expenditure within the Council. The second suite of indicators detailed below assesses the affordability of capital investment plans and the impact of capital decisions on the Council's overall finances.

The indicator the **Ratio of Financing Costs to Net Revenue Stream** demonstrates the trend in the cost of capital against the Total Revenue amount to be met from local taxpayers and the amount provided by the Assembly in the form of Revenue Support Grant. The estimates of capital financing costs include interest payable and receivable on Treasury Management activities and the Minimum Revenue Provision charged to the Comprehensive Income and Expenditure Statement. The revenue stream is the amount to be met from government grants and local taxpayers.

No.	Prudential Indicators for Affordability	2013-14 Proj.	2014-15 Est.	2015-16 Est.	2016-17 Est.	2017-18 Est.
7.	**Estimate - Ratio of Financing Costs to Net Revenue Stream**	5.02%	5.34%	5.62%	5.81%	5.77%
	Ratio	**5.02%**	**5.34%**	**5.62%**	**5.81%**	**5.77%**

The indicator of the **Incremental Impact of Capital Investment Decisions on Council Tax** identifies the estimate of the incremental impact to the Council Tax from the capital expenditure proposals, particularly changes in borrowing requirements that have occurred since the Capital Programme was approved for the year. This is a purely notional calculation designed to show the effect of changes in capital investment decisions

No.	Incremental Impact of Capital Investment Decisions on Council Tax	2013-14	2014-15 Est.	2015-16 Est.	2016-17 Est.	2017-18 Est.
8.	**Estimate - Increase in Band D Council Tax as per Capital Programme**	£ 1.65	£ 3.28	£ 3.85	£ 3.85	£ 3.85

Schedule C

ANNUAL MINIMUM REVENUE PROVISION STATEMENT 2014-15

The Annual Minimum Revenue Provision Statement needs to be approved by Council before the start of each financial year. The MRP charges for 2014-15 will be on the following bases:-

i. Capital expenditure incurred before 1 April 2008 and any capital expenditure after 1 April 2008 that is government supported expenditure and does not result in a significant asset will be based on the Capital Financing Requirement after accounting adjustments at 4% of the opening balance. This charge was supplemented by voluntary MRP (based on the useful asset life) in respect of those assets which were financed by unsupported borrowing before 1 April 2008,

ii. all unsupported capital expenditure, exercised under the Prudential Code, and supported capital expenditure that results in a significant asset incurred on or after 1 April 2008, the MRP charge will be based on the Asset Life Method. The minimum revenue provision will be at equal annual instalments over life of asset and will be met from existing budgets. The first charge can be delayed until the year after the asset is operational but this will be at the discretion of the Section 151 Officer, and

iii. for assets reclassified as finance leases under International Financial Reporting Standards (IFRS) or resulting from a Private Finance Initiative, the MRP charge will be regarded as met by a charge equal to the element of the rent/charge that goes to write down the balance sheet liability for the year and the charge will be met from existing budgets.

The MRP Charge 2014-15 based on the estimated capital financing requirement is detailed below:

	Options	Estimated Capital Financing Requirement 01-04-14 £'000	2014-15 Estimated MRP £'000
Capital expenditure before 01-04-2008 and any after 01-04-2008 that does not result in a significant asset	(i)		
(Supported)		126,638	5,062
Capital Expenditure before 01-04-2008 (Unsupported)		1,631	271
Unsupported capital expenditure, exercised under the Prudential Code, and supported capital expenditure that results in a significant asset, incurred on or after 1 April 2008	(ii)		
(Supported)		3,946	131
(Unsupported)		24,877	1,420
PFI, Finance Leases and other arrangements	(iii)		
PFI School		19,776	476
Finance Leases		41	41
Innovation Centre		816	47
Halo Leisure		1,267	117
TOTAL		**178,992**	**7,565**