BRIDGEND COUNTY BOROUGH COUNCIL

REPORT TO AUDIT COMMITTEE

15 JANUARY 2015

REPORT OF THE CORPORATE DIRECTOR – RESOURCES

TREASURY MANAGEMENT HALF YEAR REPORT 2014-15 AND TREASURY MANAGEMENT STRATEGY 2015-16

1. Purpose of the Report

1.1 The purpose of the report is to present the:

- Half Year Treasury Management report which was approved by Council on 12 November 2014;
- Proposed Treasury Management Strategy for 2015-16, which includes the:-
  - Borrowing Strategy 2015-16
  - Investment Strategy 2015-16
  - Treasury Management and Prudential Indicators for the period 2015-16 to 2018-19
  - Annual Minimum Revenue Provision Statement 2015-16

2. Connection to Corporate Improvement Objectives/Other Corporate Priorities

2.1 The work of the Audit Committee supports corporate governance and assists in the achievement of all corporate and service objectives. Prudent treasury management arrangements will ensure that investment and borrowing decisions made by officers on behalf of the Council make best use of financial resources and hence assist achievement of corporate priorities.

3. Background

3.1 The Audit Committee has delegated responsibility for ensuring effective scrutiny of the treasury management strategy and policies.

3.2 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice for Treasury Management, which was formally adopted by the Council in February 2012, requires all Local Authorities to conduct a mid-year review of its treasury management policies, practices and activities and a report was presented to Council 12 November 2014 **(Appendix A)**. As a result of this review for 2014-15, it was not deemed necessary to make any changes to the main parts of the Treasury Management Strategy 2014-15, however, it was beneficial for the Council to make some minor revisions to the Investment Strategy included within this Statement (section 5 of the Treasury Management Strategy) to enable increased flexibility in an ever changing financial market and increase the investment opportunities available to the Council whilst still maintaining security. Following consultation with the Council's Treasury advisor, Arlingclose, the changes approved by Council were:

- to include a category for UK banks and building societies rated BBB+ for investments up to 100 days with an individual counterparty limit of £2m

- reduce the unrated building society limit from assets greater than £500 million to £250million

- to ensure there is sufficient headroom within the non-specified investment limit, by increasing the investment limit to cover potential investment in the major UK banks if their credit ratings fall

An extract of the revised Investment Strategy 2014-15 incorporating all the changes are highlighted and shown in Appendix A - Schedule C**.**

3.3 The Council manages its Treasury Management activities in accordance with the Local Government Act 2003, and associated guidance:-

- The CIPFA Treasury Management in the Public Services: Code of Practice 2011 Edition (the Code), requires the Council to approve a Treasury Management Strategy (TMS) before the start of each financial year (TMS 2015-16 in **Appendix B**)

- The Welsh Government (WG) issued revised Guidance on Local Authority Investments in April 2010, which requires the Council to approve an Investment Strategy prior to the start of each financial year (Appendix B-Section 5)

- In addition to the CIPFA Code which requires treasury management indicators to be set, CIPFA's Prudential Code for Capital Finance in Local Authorities 2011 Edition requires the Council to set a number of Prudential Indicators (Appendix B-Schedule A)

- The Local Authority (Capital Finance and Accounting) (Amendment) (Wales) Regulations 2008, requires the Council to produce an Annual Minimum Revenue Provision (MRP) Statement that details the methodology for the MRP charge (Appendix B-Schedule B)

4. Current Situation / Proposal

4.1 The Treasury Management Strategy for 2015-16 (Appendix B) confirms the Council's compliance with the Code, which requires that formal and comprehensive objectives, policies and practices, strategies and reporting arrangements are in place for the effective management and control of Treasury Management activities, and that the effective management and control of risk are the prime objectives of these activities.

4.2 The Treasury Management Strategy is to be presented to Council for approval in February 2015 and whilst the main body of the report will remain unchanged there may be variations to some of the figures in the report if there are any changes (such as the capital programme) to reflect the most up to date information.

5. Effect upon Policy Framework & Procedure rules

5.1 Paragraph 17.3 of the Financial Procedure Rules within the Council's Constitution requires that all investments and borrowing transactions shall be undertaken in accordance with the Council's Treasury Management Strategy.

5.2 This report is designed to promote compliance with the above requirements.

6. Equality Impact Assessment

6.1 There are no equality implications.

7. Financial Implications

7.1 These are reflected within the report.

8. Recommendation

8.1 That members note the Half-Year Treasury Management Report which was approved by Council in November 2014;

8.2 That Members give due consideration to the Treasury Management Strategy 2015-16 before it is presented to Council for approval in February 2015 as part of the Medium term Financial Strategy.

Ness Young
Corporate Director - Resources
31 December 2014

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Background documents
CIPFA Code of Practice on Treasury Management in Local Authorities (2011)
CIPFA The Prudential Code for Capital Finance in Local Authorities (2011)

Appendix A

BRIDGEND COUNTY BOROUGH COUNCIL

REPORT TO COUNCIL

12 NOVEMBER 2014

REPORT OF THE SECTION 151 OFFICER

HALF-YEAR TREASURY MANAGEMENT REPORT 2014-15

1. Purpose of the Report

1.1 The purpose of the report is to:-

- Comply with the requirement of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services: Code of Practice 2011 Edition (the Code) to report as part of a mid-year review an overview of treasury activities;

- Report on the projected Treasury Management and Prudential Indicators for 2014-15;

- Inform Cabinet of the proposed changes to the Investment Strategy 2014-15 included in the Treasury Management Strategy.

2. Connection to Corporate Improvement Objectives / Other Corporate Priorities

2.1 The Treasury Management Report is integral to the delivery of the Corporate Improvement Objectives as the allocation of resources determines the extent to which the corporate objectives can be delivered.

3. Background

3.1 The Council's Treasury Management activities are regulated by the Local Government Act 2003 which provides the powers to borrow and invest as well as providing controls and limits on this activity. The Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003 as amended, develops the controls and powers within the Act.

3.2 The Council is required to operate the overall treasury function with regard to the Code and this was formally adopted by the Council in February 2012. This includes a requirement for the Council to approve a Treasury Management Strategy (TMS) before the start of each financial year which sets out the Council's and Chief Financial Officer's responsibilities, delegation, and reporting arrangements. Council approved the TMS 2014-15 on 19 February 2014.

3.3 The Welsh Government (WG) issued revised Guidance on Local Authority Investments in April 2010, which requires the Council to approve an

Investment Strategy prior to the start of each financial year and this is included in the TMS.

3.4 The Council is also required to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities. The Council's adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a low risk approach.

3.5 This report covers the following areas:

- The Council's treasury position for the period 1 April to 30 September 2014
- Borrowing and Debt Strategy 2014-15
- Borrowing Outturn for the period 1 April to 30 September 2014
- Investment Strategy 2014-15
- Investment Outturn for the period 1 April to 30 September 2014
- Review of the Treasury Management Strategy 2014-15
- Treasury Management and Prudential Indicators 2014-15

4. Current Situation

4.1.1 The treasury position for 1 April to 30 September 2014:

		Principal as at 01-04-14 £m	Average Rate %	Principal as at 30-09-14 £m	Average Rate %
Fixed rate long term funding	PWLB*	77.63	4.70	77.62	4.70
Variable rate long term funding	PWLB*	-	-	-	-
	LOBO**	19.25	4.65	19.25	4.65
Total Long Term External Borrowing* **		**96.88**	**4.69**	**96.87**	**4.69**
Other Long Term Liabilities*** (including PFI)		21.60		21.26	
TOTAL GROSS DEBT		**118.48**		**118.13**	
Fixed rate investments		4.50	0.63	22.00	0.48
Variable rate investments		6.00	0.55	2.40	0.50
TOTAL INVESTMENTS******		**10.50**	**0.59**	**24.40**	**0.48**
TOTAL NET DEBT		**107.98**		**93.73**	

* 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 in the Statement of Accounts and also investments shown as "Cash Equivalents" in the Council's balance sheet that mature in 1 month 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

4.1.2 Details of the debt maturity on the £96.87m long term borrowing outstanding as at 30 September 2014 are detailed 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 (the next trigger date being January 2015 however it is not expected to be repaid on this date) and therefore, the Council being given the option to accept the increase or to repay the loan without incurring a penalty. The long term liabilities figure of £21.26m at 30 September 2014 includes £19.54m for the Council's Private Finance Initiative (PFI) arrangement (for the provision of a Secondary School in Maesteg).

4.1.3 It should be noted that the accounting practice required to be followed by the Council requires financial instruments in the accounts (debt and investments) to be measured in a method compliant with International Financial Reporting Standards (IFRS). The figures shown in the above table and throughout the report are based on the actual amounts borrowed and invested and so may differ from those in the Statement of Accounts which include accrued interest or are stated at fair value in different instances.

4.1.4 The Co-operative Bank is currently the Council's bank following a competitive tender exercise in 2012. They are currently rated below the minimum credit rating identified in the Investment Strategy however a bank retendering exercise has been done and contract implementation started in October 2014 with new banking services with Barclays Bank effective from January 2015. 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 so this mitigates any potential risk associated with their drop in credit ratings.

4.1.5 The Council's Treasury Management Advisors are currently Arlingclose and the services provided to the Council include:-

- advice and guidance on relevant policies, strategies and reports,
- advice on investment decisions,
- notification of credit ratings and changes,
- other information on credit quality,
- advice on debt management decisions,
- accounting advice,
- reports on treasury performance,
- forecasts of interest rates, and
- training courses.

4.2 Borrowing and Debt Strategy for 2014-15 (Extract from TMS 2014-15)

4.2.1 <u>The Expectation for Interest Rates</u>

The interest rate views, incorporated in the Council's Treasury Management Strategy for 2014-15, were based upon officers' views supported by a selection of City forecasts provided by Arlingclose, our Treasury Management advisers.

This view was seeing the Bank Rate remaining at 0.50% for 2014-15 and it was considered that it could be 2016 before official UK interest rates rise.

4.2.2 <u>The Adopted Borrowing and Debt Strategy 2014-15</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 £5 million 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.

4.3 Borrowing Outturn for 1 April to 30 September 2014

4.3.1 The Bank Rate started the financial year at 0.50% and remained at that level from 1 April to 30 September 2014. It is forecast that it will remain at that level for the remainder of the 2014-15 financial year.

4.3.2 The Council's primary objective for the management of its debt is to ensure its long term affordability. The majority of its loans have therefore been borrowed from the Public Works Loan Board (PWLB) at long term fixed rates of interest.

4.3.3 No long or short term borrowing has been taken during the period 1 April to 30 September 2014. It was originally forecast that £5 million new PWLB borrowing would be taken in 2014-15, however, this is currently being reviewed and an update will be provided in the Cabinet report in February 2015. Market conditions have meant that there has been no loan rescheduling so far this year, however, during the second half of 2014-15, in conjunction with Arlingclose, the loan portfolio will be reviewed for any potential savings as a result of any loan rescheduling.

4.3.4 During the second half of the year, there is a potential that the Council will be receiving two loans from Welsh Government in respect of housing grants and regeneration works. These loans would be on an interest free basis repayable to Welsh Government in accordance with prescribed terms and conditions. These will be incorporated within Other Long Term Liabilities as and when they are received by the Council.

4.4 Investment Strategy 2014-15 (Extract from TMS 2014-15)

4.4.1 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.

The Annual Investment Strategy incorporated in the Council's Treasury Management Strategy 2014-15 deals with the credit ratings defined for each category of specified investments, the prudential use of non-specified investments and the liquidity of investments.

4.4.2 The Council uses long-term credit ratings from the three main rating agencies Fitch Ratings Ltd., Moody's Investors Service Inc. and Standard & Poor's Financial Services LLC to assess the risk of investment default. The lowest available credit rating will be used to determine credit quality unless an investment specific rating is available. In the current climate, relying mainly on credit ratings is considered to be inappropriate and 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.

4.4.3 A half year review of the Annual Investment Strategy will be undertaken and any changes will be reported to Council.

4.5 Investment Outturn for 1 April to 30 September 2014

4.5.1 On a day to day basis the Council typically has surplus cash balances arising from the cash flow e.g. timing differences between grants being received and making various payments. These are invested on the market via brokers, direct with the institution or held in instant access deposit accounts. The Council usually invests for a range of periods dependent on cash flow requirements and the interest rates on offer having regard to the Investment Strategy. There was one long term investment (duration of 12 months or more) taken out in April 2014 for one year but all other investments in the first half of 2014-15 were short term (instant access deposit account or fixed term deposits). The table below details these investments by counterparty type:

Investment Counterparty Category	Balance 01 April 2014 (A) £m	Investments Raised (B) £m	Investments Repaid (C) £m	Balance 30 Sept 2014 (A+B-C) £m	Average Balance Apr - Sept 2014 £m	Average Rate for Apr - Sept 2014 %
UK Government (DMO)	0.50	104.35	104.85	**0.00**	**5.74**	**0.25**
UK Local Authorities	0.00	41.30	28.30	**13.00**	**8.05**	**0.31**
Building Societies	2.00	8.00	5.00	**5.00**	**4.46**	**0.51**
Banks Call Accounts (Instant Access)	6.00	29.45	33.05	**2.40**	**5.55**	**0.50**
Banks (Fixed Maturity)	2.00	6.00	4.00	**4.00**	**4.89**	**0.76**
Total	**10.50**	**189.10**	**175.20**	**24.40**	**28.69**	**0.44**

4.5.2 Occasionally, other investments are placed with the UK Debt Management Office (DMO - Executive Agency of UK Government) but only for very short term deposits. The interest rates offered by this facility are lower than some other counterparties but this is commensurate with the high level of security and reduced risk offered. It provides another option when examining potential investments and ensures compliance with the Council's investment objective that security takes priority over yield.

4.5.3 Favourable cash flows have provided positive cash balances for investment and as shown above the balance on investments at 30 September 2014 was £24.40 million. The table below shows a breakdown based on the maturity profile and counterparty type from 30 September 2014.

Counterparty Category	Instant Access Deposit Accounts @ 30-9-14 £m	Deposits Maturing Within 1 Month @ 30-9-14 £m	Deposits Maturing Within 1-3 Months @ 30-9-14 £m	Deposits Maturing Within 4-6 Months @ 30-9-14 £m	Deposits Maturing Within 6-9 Months @ 30-9-14 £m	Total 30-9-14 £m
UK Banks	2.40	-	-	2.00	2.00	6.40
UK Building Societies	-	-	3.00	-	2.00	5.00
Local Authorities	-	9.00	-	4.00	-	13.00
Total	**2.40**	**9.00**	**3.00**	**6.00**	**4.00**	**24.40**

4.5.4 The Council's primary objective for the management of its investment portfolio is to give priority to the security and liquidity of its funds before seeking the best rate of return. As shown above, the majority of its surplus cash has been held as short term investments with UK Local Authorities and banks and building societies of high credit quality. This has therefore resulted in more of the investment portfolio being moved into investment instruments with lower rates of return but higher security and liquidity.

4.6 Review of the Treasury Management Strategy 2014-15

4.6.1 Cipfa's Code of Practice for Treasury Management requires all Local Authorities to conduct a mid-year review of its treasury management policies, practices and activities. As a result of this review it was not deemed necessary to make any changes to the main parts of the Treasury Management Strategy 2014-15, however, it would be beneficial for the Council to make some minor revisions to the Investment Strategy included within this Statement (section 5 of the Treasury Management Strategy) to enable increased flexibility in an ever changing financial market and increase the investment opportunities available to the Council whilst still maintaining security.

4.6.2 The UK is implementing the final bail-in provisions of the EU *Bank Recovery and Resolution Directive* to commence in January 2015, a year ahead of most other countries which means there a lower likelihood that the UK and other governments will support failing banks. Credit rating agencies have stated they plan to review EU banks' ratings in line with each country's implementation of the directive. Many UK banks have standalone ratings in the "BBB" category, with uplifts for potential government support taking them into the "A" category. There is therefore a realistic risk that some major UK banks' credit ratings will fall below the Council's definition of "high credit quality" of A- in this financial year if this uplift is removed. Whilst we are not considering lowering our definition on high credit quality below A-, we are proposing to amend the Investment Strategy 2014-15 to allow investment in the major UK banks as a precautionary measure.

Following consultation with Arlingclose the proposed changes are:

- to include a category for UK banks and building societies rated BBB+ for investments up to 100 days with an individual counterparty limit of £2m

- reduce the unrated building society limit from assets greater than £500 million to £250million

- to ensure there is sufficient headroom within the non-specified investment limit, by increasing the investment limit to cover potential investment in the major UK banks if their credit ratings fall

4.6.3 An extract of the revised Investment Strategy 2014-15 incorporating all the proposed changes are highlighted and shown in **Schedule C.** When the 2015-16 Treasury Management Strategy is presented to Council as part of the Medium Term Financial Strategy in February 2015 we will update Members on the new regulatory framework and how changes to the regulatory framework can best be mitigated. Maintaining a balanced investment portfolio focusing on security, liquidity and yield will still remain the Council's objective for its investments.

4.7 Treasury Management and Prudential Indicators 2014-15

4.7.1 The Treasury Management Code and Prudential Code require the Council to set and report on a number of Treasury Management and Prudential Indicators. The indicators either summarise the expected activity or introduce limits upon the activity, and reflect the underlying capital programme. **Schedule B** details the estimate for 2014-15 set out in the Council's Treasury Management Strategy and also the projected indicators for 2014-15.

5. Effect upon Policy Framework and Procedure Rules

5.1 As required by Financial Procedure Rule 17.3, all investments and borrowing transactions have been undertaken in accordance with the Treasury Management Strategy 2014-15 approved by Council.

6. Equality Impact Assessment

6.1 There are no equality implications.

7. Financial Implications

7.1 The financial implications are reflected within the report.

8. Recommendation

8.1 **It is recommended that**:

- Council approve the changes to the Investment Strategy within the Treasury Management Strategy 2014-15 as highlighted in the report and **Schedule C**;
- Council note the treasury management activities for the first half of 2014-15;
- Council note the projected Treasury Management and Prudential Indicators for 2014-15.

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21 October 2014

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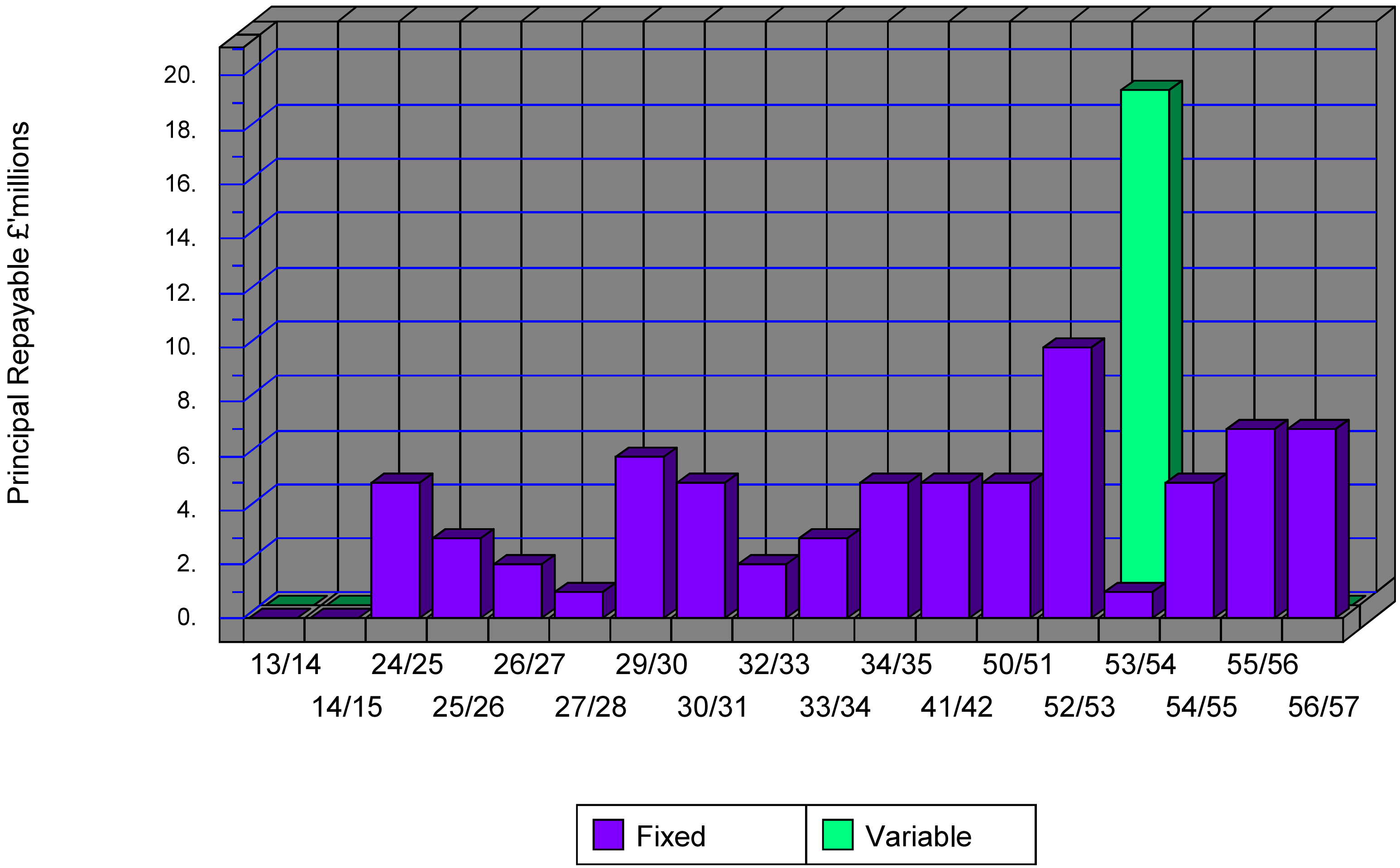
Background documents:
Treasury Management Strategy 2014-15

Schedule A
Long Term Debt Outstanding – Principal due to be paid

MATURITY ANALYSIS - 2014 to 2057



Schedule B

1 TREASURY MANAGEMENT INDICATORS 2014-15

1.1.1 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	Treasury Management Strategy 2014-15 £m	Projection 31-03-2015 £m
	Total Projected Principal Outstanding on Borrowing 31 March 2015	101.87	**101.87**
	Total Projected Principal Outstanding on Investments 31 March 2015	9.00	**9.00**
	Net Principal Outstanding	**92.87**	**92.87**
1.	**Upper Limit on fixed interest rates (net principal) exposure**	130.00	**80.62**
2.	**Upper Limit on variable interest rates (net principal) exposure**	50.00	**12.25**

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

1.1.2 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. The Code requires the maturity of LOBO loans to be shown as the earliest date on which the lender can require payment, i.e. the next call date of January 2015 (which is shown below), however it is not expected that the loans will repaid on that date.

No	Maturity structure of fixed rate borrowing during 2014-15	Upper limit	lower limit	Projection 2014-15
3.	Under 12 months	50%	0%	**18.91%**
	12 months and within 24 months	25%	0%	**0.02%**
	24 months and within 5 years	50%	0%	**0.00%**
	5 years and within 10 years	60%	0%	**0.00%**
	10 years and above	100%	40%	**81.07%**

1.1.3 The **Upper Limit for Total Principal Sums invested over 364 days** indicator 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.		Treasury Management Strategy 2014-15 (Limit) £m	Projection 31-03-15 £m
4.	**Upper Limit for Total Principal Sums Invested for more than 364 days**	12	**4**

2 PRUDENTIAL INDICATORS 2014-15

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.

2.1 Prudential Indicators for Prudence

2.1.1 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	Estimate Treasury Management Strategy 2014-15 £'000	Projection 31-03-15 £'000
1	**Estimates of Capital Expenditure**		
	Non – HRA	32,060	29,685
	Total Capital Expenditure	**32,060**	**29,685**
	Financed by :-		
	Capital Grants and Contributions	11,393	9,933
	Capital Receipts	12,005	9,748
	Revenue	0	38
	Net Financing Need for Year	**8,662**	**9,966**

The capital expenditure figures have changed from the Treasury Management Strategy 2014-15 as the capital programme approved by Council on 19 February 2014 has been amended to include new approved schemes, to incorporate slippage of schemes identified as part of the capital monitoring and a change in the profile of prudential borrowing. This has resulted in an increase in the Net Financing Need for 2014-15.

2.1.2 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 financing of capital expenditure to revenue is a statutory requirement and is called the Minimum Revenue Provision (MRP).The actual MRP charge needs to be prudent and the methodology has been revised from 2014-15 as detailed in the Council's MRP policy in the TMS 2014-15. The MRP requirement for the PFI Scheme, Finance Leases, Innovation Centre and HALO will be equivalent to the write down of the liability for the year and is met from existing budgets.

No.	Prudential indicators For Prudence	Est. Treasury Management Strategy 2014-15 £'000	Projection 2014-15 £'000
2	**Capital Financing Requirement (CFR)**		
	Opening CFR (1 April 2014) excluding PFI	157,092	155,429
	Opening PFI CFR	19,776	19,776
	Opening Finance Lease CFR	41	41
	Opening Innovation Centre	816	816
	Opening HALO	1,267	971
	Total Opening CFR	**178,992**	**177,033**
	Movement in CFR excluding PFI & other liabilities	1,778	3,135
	Movement in PFI CFR	(476)	(476)
	Movement in Finance Lease CFR	(41)	(41)
	Movement in Innovation Centre CFR	(47)	(47)
	Movement in HALO CFR	(117)	180
	Total Movement in CFR	**1,097**	**2,751**
	Closing CFR (31 March 2015)	**180,089**	**179,784**
	Movement in CFR represented by :-		
	Net Financing Need for Year (above)	8,662	9,966
	Adjustment for Halo	-	296
	Minimum and Voluntary Revenue Provisions*	(7,565)	(7,511)
	Total Movement	**1,097**	**2,751**

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

2.2 Limits to Borrowing Activity

2.2.1 The Council's long term borrowing at the 30 September 2014 was £96.87m as detailed in section 4.1.1 the Treasury Position. 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	Estimate Treasury Management Strategy 2014-15 Est. £'000	Projection 31-03-15 £'000
3	External Borrowing	101,867	101,867
	Long Term Liabilities (including PFI)	21,219	21,219
	Total Gross Debt	**123,086**	**123,086**

2.2.2 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. The table below shows that the Council is on target to comply with this requirement.

No.	Prudential indicators For Prudence	Estimate Treasury Management Strategy 2014-15 £'000	Projection 31-03-15 £'000
4	**Gross Debt & the CFR**		
	Total Gross Debt	123,086	123,086
	Closing CFR (31 March 2015)	**180,089**	**179,784**

2.2.3 A further two Prudential Indicators control the Council's overall level of debt to support capital expenditure. These are detailed below and confirms that the Council is well within the limit set :-

- 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.

Prudential Indicators for Prudence Nos. 5 & 6	Authorised Limit Treasury Management Strategy 2014-15 £m	Operational Boundary Treasury Management Strategy 2014-15 £m	Projection 31-03-15 £m
Borrowing	140	115	102
Other long term liabilities	30	25	21
Total	**170**	**140**	**123**

2.3 Prudential Indicators for Affordability

2.3.1 The Prudential Code Indicators Numbered 1 to 6 above in section 2.1 and 2.2 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 Welsh Government 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	Estimate Treasury Management Strategy 2014-15	Projection 2014-15
7.	**Ratio of Financing Costs to Net Revenue Stream**		
	Ratio	5.34%	**5.10%**

2.3.2 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	Estimate Treasury Management Strategy 2014-15	Projection 2014-15
8.	Increase in Band D Council Tax as per Capital Programme	£ 3.28	£ **2.96**

Schedule C

Proposed Extract to be inserted into Treasury Management Strategy 2014-15 (Section 5.0)

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.

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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 £250m)	£ 6m
Total investments (excluding building societies – separate limit above) not meeting the Council's high credit quality definition	£ 6m

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- BBB+	2 years 1 year 1 year 6 months 100 days	£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) £2m
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 £250m		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).

Appendix B

TREASURY MANAGEMENT STRATEGY 2015-16

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.

The Co-Operative Bank announced in November 2013 that it did not wish to support local government banking beyond 2015-16 so a bank retendering exercise was undertaken in 2014 and a new banking contract has been awarded to Barclays Bank which commenced on 5 January 2015.

2.0 Economic Context and Forecasts for Interest Rates

Economic background: There is momentum in the UK economy, with a continued period of growth through domestically-driven activity and strong household consumption. There are signs that growth is becoming more balanced. The greater contribution from business investment should support continued, albeit slower, expansion of Gross Domestic Product. However, inflationary pressure is benign and is likely to remain low in the short-term. There have been large falls in unemployment but levels of part-time working, self-employment and underemployment are significant and nominal earnings growth remains weak and below inflation.

The Bank of England's Monetary Policy Committee (MPC)'s focus is on both the degree of spare capacity in the economy and the rate at which this will be used up, factors prompting some debate on the Committee. Despite two MPC members having voted for a 0.25% increase in rates at each of the meetings August 2014 onwards, some Committee members have become more concerned that the economic outlook is less optimistic than at the time of the August *Inflation Report*.

Credit outlook: The transposition of two European Union directives into UK legislation in the coming months will place the burden of rescuing failing EU banks disproportionately onto unsecured local authority investors. The *Bank Recovery and Resolution Directive* promotes the interests of individuals and small businesses covered by the Financial Services Compensation Scheme and similar European schemes, while the recast *Deposit Guarantee Schemes Directive* includes large companies into these schemes. The combined effect of these two changes is to leave public authorities and financial organisations (including pension funds) as the only senior creditors likely to incur losses in a failing bank after July 2015.

The continued global economic recovery has led to a general improvement in credit conditions since last year. This is evidenced by a fall in the credit default swap spreads of banks and companies around the world. However, due to the above legislative changes, the credit risk associated with making unsecured bank deposits will increase relative to the risk of other investment options available to the Council. This has led to a requirement for the Council to adopt a new strategy for 2015-16 which is detailed in section 5 Investment Strategy.

Interest rate forecast: The Council's treasury management advisor Arlingclose forecasts the first rise in official interest rates in August 2015 and a gradual pace of increases thereafter, with the average for 2015-16 being around 0.75%. Arlingclose believes the normalised level of the Bank Rate post-crisis to range between 2.5% and 3.5%. The risk to the upside (i.e. interest rates being higher) is weighted more towards the end of the forecast horizon. On the downside, Eurozone weakness and the threat of deflation have increased the risks to the durability of UK growth. If the negative indicators from the Eurozone become more entrenched, the Bank of England will likely defer rate rises to later in the year. Arlingclose projects gilt yields on an upward path in the medium term, taking the forecast average 10 year PWLB loan rate for 2015-16 to 3.40%.

Arlingclose (Council's TM Advisers) central interest rate forecast – December 2014

	Bank Rate	3 Bank month LIBID	1 Year LIBID	5-year gilt yield	10 year gilt yield	20-year gilt yield*	50-year gilt yield*
Dec 2014	0.50	0.55	0.95	1.70	2.40	2.90	3.00
Mar 2015	0.50	0.60	1.00	1.75	2.45	2.95	3.05
June 2015	0.50	0.65	1.05	1.90	2.55	3.05	3.10
Sept 2015	0.75	0.85	1.20	2.00	2.60	3.10	3.15
Dec 2015	0.75	1.00	1.35	2.10	2.65	3.15	3.20
Mar 2016	1.00	1.15	1.50	2.20	2.70	3.20	3.25
June 2016	1.00	1.30	1.65	2.30	2.75	3.25	3.30
Sept 2016	1.25	1.45	1.80	2.40	2.80	3.30	3.35
Dec 2016	1.25	1.60	1.95	2.50	2.85	3.35	3.40
Mar 2017	1.50	1.75	2.10	2.60	2.90	3.40	3.45
Jun 2017	1.50	1.85	2.20	2.70	2.95	3.45	3.50
Dec 2017	1.75	2.05	2.40	2.90	3.05	3.50	3.55
Mar 2017	1.75	2.15	2.50	2.95	3.10	3.55	3.60

3.0 The Council's Current Treasury Management Position

The Council's debt and investment position as at 29 December 2014 is shown below:

Table 1

		Principal as at 29-12-14 £m	Average Rate %
Fixed rate long term funding	PWLB(i)	77.62	4.70
Variable rate long term funding	PWLB	-	-
	LOBO(ii)	19.25	4.65
Total Long Term External Borrowing(iii)		**96.87**	**4.69**
Other Long Term Liabilities(iii) (including PFI)		21.32	
TOTAL GROSS DEBT		**118.19**	
Fixed rate investments (iv)		21.00	0.52
Variable rate investments		5.40	0.46
TOTAL INVESTMENTS(v)		**26.40**	**0.51**
TOTAL NET DEBT		**91.79**	

(i) Public Works Loan Board (PWLB)
(ii) Lender's Option Borrower's Option (LOBO)

(iii) Long term borrowing/liabilities include all instruments with an initial term of 365 days or more.
(iv) Fixed rate in the above table includes instruments which are due to mature in the year
(v) The investment totals include instant access deposit accounts which are included as “Cash” in the Council’s balance sheet in the Statement of Accounts and also investments shown as “Cash Equivalents” in the Council’s balance sheet that mature in 1 month or less from the date of acquisition and that are readily convertible to known amounts of cash with insignificant risk of change in value

The £19.25m relates to Lender’s Option Borrower’s Option (LOBO) loans which have a maturity date of 2054, however these 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 January 2015 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 in the future.

Investments are anticipated to drop from £26.40m on 29 December 2014 to approximately £9m by the 31 March 2015. This is due partly to the reduction in income collected from Council Tax and National Non-Domestic Rates in February and March 2015 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 A** which shows that the Council expects to comply with this recommendation during 2015-16 and the following three years.

4.0 Borrowing Strategy

The major **objectives** to be followed in 2015-16 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 ,
- 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 2015-16 is £5m at an estimated rate of 4.00%.

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 A.**

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 and Welsh Government (WG)
- 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 Welsh Government and 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 and revenue implications of repaying the loan,
- 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.

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 2015-16 to range from £5m to £40m with an average investment rate of 0.45% (based on current rates and investment types) but this will be reviewed at half year and reported to Council. 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).

The major **objectives** to be followed in 2015-16 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.

The Council's investments have historically been placed in short term bank and building society unsecured deposits and local and central government, however, investments may be made with any public or private sector organisations that meet the credit criteria detailed below. This change is included in the Strategy as there is increasing (relative) risk from short-term unsecured bank and building society investments therefore requiring the Council to diversify into more secure and/or higher yielding asset classes during 2015-16. 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. As this diversification will represent a substantial change in approach, appropriate training will be provided by the Council's treasury management advisers before investments are made in these alternative instruments. Any new instruments used will be in full consultation with these advisers.

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.

Credit Rating: Investment decisions are made by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used.

Approved Counterparties: The Council may invest with any of the counterparty types shown below in Table 2 below, subject to the cash limits (per counterparty) and the time limits shown. **These must be read in conjunction with the notes immediately below the table and the combined secured and unsecured investments in any one bank must not exceed the cash limit for secured investments**:

Table 2: Approved Counterparties

Credit Rating	Banks (including building societies) Unsecured	Banks (including building societies) Secured	Government	Corporates	Registered Providers
UK Central Government	N/A	N/A	£ Unlimited 50 Years	N/A	N/A
UK Local Authorities *	N/A	N/A	£15,000,000 10 Years	N/A	N/A
AAA	£3,000,000 5 Years	£4,000,000 20 Years	£4,000,000 50 Years	£2,000,000 20 Years	£2,000,000 20 Years
AA+	£3,000,000 5 Years	£4,000,000 10 Years	£4,000,000 25 Years	£2,000,000 10 Years	£2,000,000 10 Years
AA	£3,000,000 4 Years	£4,000,000 5 Years	£4,000,000 15 Years	£2,000,000 5 Years	£2,000,000 10 Years
AA-	£3,000,000 3 Years	£4,000,000 4 Years	£4,000,000 10 Years	£2,000,000 4 Years	£2,000,000 10 Years
A+	£3,000,000 2 Years	£4,000,000 3 Years	£2,000,000 5 Years	£2,000,000 3 Years	£2,000,000 5 Years
A	£3,000,000 13 Months	£4,000,000 2 Years	£2,000,000 5 Years	£2,000,000 2 Years	£2,000,000 5 Years
A-	£3,000,000 6 Months	£4,000,000 13 Months	£2,000,000 5 Years	£2,000,000 13 Months	£2,000,000 5 Years
BBB+	£1,000,000 100 Days	£2,000,000 6 Months	£1,000,000 2 Years	£1,000,000 6 Months	£1,000,000 2 Years
BBB or BBB-	£1,000,000 Next day only	£2,000,000 100 Days	N/A	N/A	N/A
None	£1,000,000 6 Months	N/A	£2,000,000 25 Years	N/A	£2,000,000 5 Years
Pooled Funds	£4,000,000 Per Fund				

** excluding parish and community councils*

Banks Unsecured: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. Unsecured investment with banks rated BBB or BBB- are restricted to overnight deposits at the Council's current account bank.

Banks Secured: Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits.

The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

Government: Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency.

Corporates: Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made as part of a diversified pool in order to spread the risk widely.

Registered Providers: Loans and bonds issued by, guaranteed by, or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Welsh Government and, as providers of public services, they retain a high likelihood of receiving government support if needed.

Money Market Funds (type of pooled fund): 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. Money Market Funds that offer same-day liquidity and aim for a constant net asset value may be used as an alternative to instant access bank accounts. To date the Council has not used money market funds.

Other Pooled Funds: The Council may consider using pooled bond, equity and property funds whose value changes with market prices and/or have a notice period will be used for longer investment periods as they offer enhanced returns over the longer term, and 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 Rating Criteria and their Use: Credit ratings are obtained and monitored by the Council's treasury advisers, who will notify changes as they occur.

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 or invested in government treasury bills 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.

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 pound 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:

- the UK Government,
- a UK local authority,
- a UK parish or community council or
- body or investment scheme of "high credit quality"

The Council's defines **"high credit quality"** organisations and securities as those 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.

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 .

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. Table 3 below shows the non-specified 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:

Table 3: Non-Specified Investment Limits

	Category Total Cash limit
Total long-term investments	£15m
Total Money Market Funds and other pooled funds	£10m
Total investments without credit ratings or rated below A-	£ 6m
Total investments with institutions domiciled in foreign countries rated below AA+	£ 3m

Investment Limits:
The combined values of specified and non-specified investments with any one organisation are subject to the investment limits detailed below in Table 4, the approved counterparties and limits shown in Table 2 above and also the non-specified limits in Table 3 above. A group of banks under the same ownership will be treated as a single organisation for limit purposes.

Table 4: Investments Limits

	Cash limit
Any single organisation, except the UK Central and Local Government	£4m
UK Central Government	unlimited
UK Local Authorities	£15m
Any group of organisations under the same ownership	£4m per group
Any group of pooled funds under the same management	£4m per manager
Negotiable instruments held in a broker's nominee account	£10m per broker
Foreign countries	£4m per country
Registered Providers	£5m in total
Unsecured investments with Building Societies	£5m in total

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 A** revises some of the indicators for 2014-15, 2015-16, 2016-17, 2017-18 and introduces new indicators for 2018-19 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 2015-16

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 B.**

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 can be 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 pooled funds 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 2015, was in excess of the actual debt of the Council. 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

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 Proj £m	2015-16 Est. £m	2016-17 Est. £m	2017-18 Est. £m	2017-18 Est. £m
	Total Projected Principal Outstanding on Borrowing 31 March	**96.87**	101.87	106.87	111.87	116.87
	Total Projected Principal Outstanding on Investments 31 March	9.00	8.00	7.00	6.00	5.00
	Net Principal Outstanding	**87.87**	**93.87**	**99.87**	**105.87**	**111.87**
1.	**Upper Limit on fixed interest rates (net principal) exposure**	130.00	140.00	145.00	150.00	155.00
2.	**Upper Limit on variable interest rates (net principal) exposure**	50.00	50.00	50.00	50.00	50.00

The Section 151 Officer will manage interest rate exposures between these limits.

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 2015-16	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** indicator 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.		2015-16 £m	2016-17 £m	2017-18 £m	2018-19 £m
4.	**Upper Limit - Total Principal Sum Invested more than 364 day days**	15	10	8	6

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	2014-15 £'000 Proj.	2015-16 £'000 Est.	2016-17 £'000 Est.	2017-18 £'000 Est.	2018-19 £'000 Est.
1	**Estimates of Capital Expenditure**					
	Non – HRA	31,350	34,983	23,509	12,315	6,575
	Total Capital Expenditure	**31,350**	**34,983**	**23,509**	**12,315**	**6,575**
	Financed by :-					
	Capital Grants and Contributions	10,153	14,715	14,538	5,104	2,414
	Capital Receipts	10,322	9,159	3,949	3,302	252
	Revenue	419	0	0	0	0
	Net Financing Need for Year	**10,456**	**11,109**	**5,022**	**3,909**	**3,909**

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 financing of 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 B.**

No.	Prudential indicators For Prudence	2014-15 £'000 Proj.	2015-16 £'000 Est.	2016-17 £'000 Est.	2017-18 £'000 Est.	2018-19 £'000 Est.
2	**Capital Financing Requirement (CFR)**					
	Opening CFR (1 April) excluding PFI	155,429	159,092	163,460	161,935	159,118
	Opening PFI CFR	19,776	19,300	18,787	18,235	17,640
	Opening Finance Lease CFR	41	0	0	0	0
	Opening Innovation Centre	816	769	719	663	603
	Opening HALO	971	1,150	1,033	917	800
	Total Opening CFR	**177,033**	**180,311**	**183,999**	**181,750**	**178,161**
	Movement in CFR excluding PFI & other liab	3,662	4,368	(1,525)	(2,817)	(2,751)
	Movement in PFI CFR	(476)	(512)	(552)	(595)	(640)
	Movement in Finance Lease CFR	(41)	0	0	0	0
	Movement in Innovation Centre CFR	(47)	(51)	(55)	(60)	(65)
	Movement in HALO CFR	180	(117)	(117)	(117)	(117)
	Total Movement in CFR	**3,278**	**3,688**	**(2,249)**	**(3,589)**	**(3,573)**
	Closing CFR (31 March)	**180,311**	**183,999**	**181,750**	**178,161**	**174,588**
	Movement in CFR represented by :-					
	Net Financing Need for Year (above)	10,456	11,109	5,022	3,909	3,909
	Adjustment for Halo	296	0	0	0	0
	Minimum and Voluntary Revenue Provisions*	(7,474)	(7,421)	(7,271)	(7,498)	(7,483)
	Total Movement	**3,278**	**3,688**	**(2,249)**	**(3,589)**	**(3,574)**

*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 29 December 2014 was £96.87m 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	2014-15 £'000 Proj.	2015-16 £'000 Est.	2016-17 £'000 Est.	2017-18 £'000 Est.	2018-19 £'000 Est.
3	External Borrowing	96,867	101,867	106,867	111,867	116,867
	Long Term Liabilities (including PFI)	21,219	20,539	19,815	19,043	18,220
	Total Gross Debt	**118,086**	**122,406**	**126,682**	**130,910**	**135,087**

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 2014-15 (i.e. the preceding year) plus the estimates of any additional capital financing requirement for the current and next three financial years, however 2018-19 has also been included to be consistent with the Medium Term Financial Strategy.

No.	Prudential indicators For Prudence	2014-15 £'000 Proj.	2015-16 £'000 Est.	2016-17 £'000 Est.	2017-18 £'000 Est.	2018-19 £'000 Est.
4	**Gross Debt & the CFR**					
	Total Gross Debt	118,086	122,406	126,682	130,910	135,087
	Closing CFR (31 March)	**180,311**	**183,999**	**181,750**	**178,161**	**174,588**

As can be seen from the above table, the Council does not have any difficulty meeting this requirement in 2014-15 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	2014-15 £m	2015-16 Est. £m	2016-17 Est. £m	2017-18 Est. £m	2018-19 Est. £m
5	**Authorised limit for external debt**					
	Borrowing	140	140	140	140	140
	Other long term liabilities	30	30	30	30	30
	Total	**170**	**170**	**170**	**170**	**170**
6	**Operational Boundary**					
	Borrowing	115	105	110	115	120
	Other long term liabilities	25	25	25	25	25
	Total	**140**	**130**	**135**	**140**	**145**

<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	2014-15 Proj.	2015-16 Est.	2016-17 Est.	2017-18 Est.	2018-19 Est.
7.	Estimate - Ratio of Financing Costs to Net Revenue Stream					
	Ratio	5.00%	5.05%	5.15%	5.45%	5.60%

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	2014-15	2015-16 Est.	2016-17 Est.	2017-18 Est.	2018-19 Est.
8.	Estimate - Increase in Band D Council Tax as per Capital Programme	£ 2.96	£ 3.85	£ 3.85	£ 3.85	£ 3.85

Schedule B

ANNUAL MINIMUM REVENUE PROVISION STATEMENT 2015-16

The Annual Minimum Revenue Provision Statement needs to be approved by Council before the start of each financial year. The MRP charges for 2015-16 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 (based on an internal assessment) 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. 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;
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;
iv. Where loans are made to other bodies for their capital expenditure with an obligation for the bodies to repay, no MRP will be charged. The capital receipts generated by the annual repayments on those loans will be put aside to repay debt instead.

The MRP Charge 2015-16 based on the estimated capital financing requirement is detailed below:-

	Options	Estimated Capital Financing Requirement 01-04-15 £'000	2015-16 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)		125,390	4,855
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)		3,932	131
(Unsupported)		28,139	1,484
PFI, Finance Leases and other arrangements	(iii)		
PFI School		19,300	512
Innovation Centre		769	51
Halo Leisure		1,150	117
TOTAL		180,311	7,421