

TREASURY MANAGEMENT STRATEGY STATEMENT and ANNUAL INVESTMENT STRATEGY 2011/2012

TREASURY MANAGEMENT STRATEGY STATEMENT

1. Introduction

The Local Government Act 2003 requires the Council to 'have regard to 'the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy (AIS) (as required by Investment Guidance issued subsequent to the Act) (included as paragraph 9). The AIS sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

The suggested strategy for 2011/12 in respect of the following aspects of the treasury management function is based upon the Treasury officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury advisors, Arlingclose Ltd. The strategy covers:

- treasury limits in force which will limit the treasury risk and activities of the Council;
- Prudential Indicators;
- the current treasury position;
- prospects for interest rates;
- the borrowing requirement;
- the borrowing strategy;
- debt rescheduling;
- the investment strategy;
- Annual MRP statement
- Other items

There is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This, therefore, means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from: -

- a) increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
- b) any increases in running costs from new capital projects are limited to a level which is affordable within the projected income of the Council for the foreseeable future.

2. Treasury Limits for 2011/12 to 2013/14

There is a statutory duty under S.3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the "Affordable Borrowing Limit".

The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax and council rent levels is 'acceptable'.

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Whilst termed an “Affordable Borrowing Limit”, the capital plans to be considered for inclusion incorporate financing by external borrowing. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and the two successive financial years.

3. Prudential Indicators for 2010/11 – 2013/14

3.1.1 The Council is also required to indicate that it has adopted the CIPFA Code of Practice on Treasury Management. This was adopted in February 2002 by full Council.

The following prudential indicators are relevant for the purposes of setting an integrated treasury management strategy.

3.1.2 The Council must estimate its total capital expenditure, split between the Housing Revenue Account (HRA) and non HRA, in the next three or more financial years. This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax and in the case of the HRA, housing rent levels.

3.1.3 The actual capital expenditure that was incurred in 2009/10 and the estimates of capital expenditure to be incurred for the current and future years that are recommended for approval are:-

Capital Expenditure					
Proposed Capital programme	2009/10 £000 Actual	2010/11 £000 Revised	2011/12 £000 Estimate	2012/13 £000 Estimate	2013/14 £000 Estimate
General Fund	2,136	3,254	7,641	4,956	1,056
HRA	4,314	3,851	4,828	3,800	4,000
Total	6,450	7,105	12,469	8,756	5,056

3.1.4 Estimates of the ratio of financing costs to the net revenue stream

This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs. It would not be prudent for borrowing costs to be a significant proportion of net revenue either now or in the future. By estimating the ratio for at least the next three years the trend in the cost of capital (borrowing costs net of interest and investment income) as a proportion of revenue income can be seen.

3.1.5 Estimates of the ratio of financing costs to net revenue stream for the current and future years, and the actual figures for 2009/10 are:

Ratio of Financing Costs to Net Revenue Stream					
	2009/10 Actual %	2010/11 Revised %	2011/12 Estimate %	2012/13 Estimate %	2013/14 Estimate %
Non-HRA	3.03%	3.77%	4.81%	5.07%	4.52%
HRA	2.55%	2.67%	2.67%	3.64%	3.60%

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3.1.6 Capital Financing Requirement

The capital financing requirement measures the authority's underlying need to borrow for a capital purpose. In accordance with best professional practice, Cheltenham Borough Council does not associate borrowing with particular items or types of expenditure. The authority has an integrated treasury management strategy and has adopted the CIPFA Code of Practice for Treasury Management in the Public Services. Cheltenham Borough Council has, at any point in time, a number of cashflows both positive and negative, and manages its treasury position in terms of its borrowings and investments in accordance with its approved treasury management strategy and practices. In day to day cash management, no distinction can be made between revenue cash and capital cash. External borrowing arises as a consequence of all the financial transactions of the authority and not simply those arising from capital spending.

3.1.7 The Council can borrow without limit, provided it ensures such borrowing is affordable, prudent and sustainable.

3.1.8 Estimates of the end of year capital financing requirement for the authority for the current and future years and the actual capital financing requirement at 31st March 2010 are:

Capital Financing Requirement (CFR)					
	31/3/10 £000 Actual	31/3/11 £000 Revised	31/3/12 £000 Estimate	31/3/13 £000 Estimate	31/3/14 £000 Estimate
Non-HRA	26,709	25,834	28,818	31,118	30,534
HRA	18,728	18,728	18,728	18,728	18,728
Total CFR	45,437	44,562	47,546	49,846	49,262

The move to International Financial Reporting Standards (IFRS) from 1 April 2010 may in future have implications for the capital expenditure and Capital Financing Requirement (CFR) indicators. This is because under IFRS all leases have to be reassessed and classified either as 'finance' or 'operating' leases. Under IFRS, finance leases in effect count as capital expenditure funded by borrowing, whereas operating leases are rental agreements, which do not affect the indicators.

Following an analysis of the council's leases at 1 April 2010, all have been classified as operating leases. However if the wheeled bins, caddies, recycling and other vehicles to be bought in 2010/11 are leased, they are likely to be classified as finance leases, counting as capital expenditure and borrowing. Given the accounting treatment of finance leases is now in effect the same as if the council undertook prudential borrowing, an assessment of the funding options for these assets is currently being undertaken.

If the assets are leased under a finance lease or if the council borrows to fund the assets, the forecast capital expenditure and CFR for 2010/11 will increase by the cost of these assets and the prudential indicators will need to be revised for future years. This will be reported as part of the Treasury Management and Revenue Outturn reports in June 2011.

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3.1.9 Net borrowing and the Capital Financing Requirement

CIPFA's Prudential Code for Capital Finance in Local Authorities includes the following as a key indicator of prudence:

"In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that the net external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years."

3.1.10 Local authorities may borrow temporarily to cover cash flow shortages but over the medium term should only borrow to finance capital expenditure.

3.1.11 In order to ensure that over the medium term net borrowing will only be for capital purposes, the Council needs to ensure its net external borrowing does not exceed its Capital Financing Requirement over the current and next three years. The table below demonstrates that the estimated level of net investments remains lower than the capital financing requirement in each year, and therefore meets this requirement.

Estimated net borrowing and capital financing requirement at Year end	2009/10 £000 Actual	2010/11 £000 Revised	2011/12 £000 Estimate	2012/13 £000 Estimate	2013/14 £000 Estimate
Gross borrowing	51,997	57,013	60,612	63,512	61,512
Investments	16,557	15,535	15,535	15,535	13,535
Net (Investment) / borrowing	35,440	41,478	45,077	47,977	47,977
Capital financing requirement	45,437	44,562	47,546	49,846	49,262

3.1.12 Estimates of the incremental impact of capital expenditure on the council tax and housing rents

A fundamental indicator of the affordability of capital expenditure plans is its impact on the council tax and housing rents. Any borrowing for capital purposes has an impact on the revenue account and, to the extent it is not supported by government or other contributions, on council tax and/or housing rents. Using capital receipts to fund capital expenditure also has an impact because the assets sold would no longer generate rental income or investment income. The use of revenue funding to fund capital clearly has a direct impact on the revenue account and council taxes/rents. The completed capital schemes will also have an impact in terms of running costs and income generated.

3.1.13 The Council must estimate the incremental impact of its capital expenditure plans (shown above) on the council tax and housing rents for the next three years or more.

3.1.14 The estimate of the incremental impact of capital investment decisions proposed in this budget report, over and above capital investment decisions that have previously been taken by the Council are:

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For the Band D Council Tax –

2011/12 £Nil*	2012/13 £Nil	2013/14 £Nil
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* As a proposed Council Tax freeze for 2011/12.

For average weekly housing rents

2011/12 Nil**	2012/13 Nil**	2013/14 Nil**
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** Decisions on annual rent increases are now subject to rent restructuring guidelines set by Central Government. As a consequence the link between rent levels and capital expenditure no longer applies.

3.2 External Debt Indicators

Two limits need to be set and monitored to ensure borrowing is prudent, affordable and sustainable.

3.2.1 Authorised Limit

The Council must set an authorised limit for its external debt for the next three financial years or more. This is

- the possible maximum level of borrowing that may need to be incurred and the limit beyond which borrowing will be prohibited
- the statutory limit specified in section 3(1) of the Local Government Act 2003
- Reflects a level of borrowing which, although affordable in the short term may not be sustainable
- The 'outer boundary' of the Council's possible need to borrow.

3.2.2 In respect of its external debt, it is recommended that the Council approves the following authorised limits for its total external debt gross of investments for the next three financial years. The Council is asked to approve these limits and to delegate authority to the Section 151 Officer, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities, in accordance with option appraisal and best value for money for the authority.

Authorised Limit for External Debt				
	2010/11 £000	2011/12 £000	2012/13 £000	2013/14 £000
Borrowing	83,000	81,000	80,000	79,000
Other long term liabilities	-	-	-	-
Total	83,000	81,000	80,000	79,000

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- 3.2.3 In setting the limit, account must be taken of the authority's current commitments, existing plans and the proposals in the budget report for capital expenditure and financing, and with its approved treasury management policy statement and practices. Risk analysis has been taken into account; as have plans for capital expenditure, estimates of the capital financing requirement and estimates of cash flow requirements.

This limit represents the worst case scenario, i.e. the effect on the cash flow of receiving no council tax income and borrowing to the maximum of the capital financing requirement, in addition to investments held. The calculation follows a prescribed formula and is in excess of the expected levels of borrowing for 2011/12 to 2013/14 in accordance with Treasury strategy and as shown in the Operational Boundary indicator in paragraph 3.2.6.

- 3.2.4 In taking its decisions on this report, the Council is asked to note that the authorised limit determined for 2011/12 the statutory limit determined under section 3(1) of the Local Government Act 2003.

3.2.5 Operational Boundary

The Council is also asked to approve the following operational boundary for external debt for the same time period. The proposed operational boundary for external debt is based on the same estimates as the authorised limit but reflects directly the estimate of the most likely, prudent but not worst case scenario, without the additional headroom included within the authorised limit to allow for example for unusual cash movements. The operational boundary represents a key management tool for in year monitoring. Within the operational boundary, figures for borrowing and other long term liabilities are separately identified. The Council is also asked to delegate authority to the Section 151 Officer, to effect movement between separately agreed figures for borrowing and other long term liabilities, in a similar fashion to the authorised limit.

- 3.2.6 The boundary may be breached occasionally due to unexpected cash flow shortages but a sustained breach would indicate the Council may be in danger of breaching the Authorised Limit. The Council is recommended to approve the following limits for this indicator.

Operational Boundary for External Debt				
	2010/11 £000	2011/12 £000	2012/13 £000	2013/14 £'000
Borrowing	67,000	71,000	74,000	72,000
Other long term liabilities	-	-	-	-
Total	67,000	71,000	74,000	72,000

- 3.2.7 The operational boundary represents the maximum expected operational borrowing at a given time, which is significantly lower than the prescribed authorised limit shown in paragraph 3.2.2. This measure reflects a more realistic view of likely cash flow scenarios, and should not be exceeded.

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3.2.8 The Council's actual external debt at 31st March 2010 was £51.997 million. It should be noted that actual external debt is not directly comparable to the authorised limit and operational boundary, since the actual external debt reflects the position at one point in time.

3.3. Upper limits on interest rate exposure

The Council must set upper limits on its exposure to changes in interest rates for at least the next three years. An upper limit must be set for both fixed and variable rates covering both borrowing and investments.

- 3.3.1 The purpose of these indicators is to reduce the likelihood of an adverse movement in interest rates or borrowing / investment decisions impacting negatively on the Council's overall financial position.
- 3.3.2 It is recommended that the Council sets an upper limit on its fixed interest rate exposures for 2011/12, 2012/13 and 2013/14 of its gross outstanding borrowing.
- 3.3.3 It is further recommended that the Council sets an upper limit on its variable interest rate exposures for 2011/12, 2012/13 and 2013/14 of 100% of its gross outstanding borrowing.
- 3.3.4 This means the Section 151 Officer will manage fixed interest rate exposures within the range 0% to 100% and variable interest rate exposures within the range 0% to 100%.

3.3.5 Maturity structure of borrowing

The Council must set both upper and lower limits with respect to the maturity structure of borrowing for the following financial year. This indicator is designed to be a control over an authority having large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates. Therefore the aim should be a relatively even spread of debt repayment dates.

3.3.6 It is recommended that the Council sets upper and lower limits for the maturity structure of its borrowings as follows:

Amount of projected borrowing that is fixed rate maturing in each period is:

	Upper Limit %	Lower Limit %
Under 12 months	50	0
12 months and within 24 months	50	0
24 months and within 5 years	100	0
5 years and within 10 years	100	0
10 years and within 20 years	100	0

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20 years and within 30 years	100	0
30 years and within 40 years	100	0
40 years and within 50 years	100	0
50 years and above	100	0

4. Current Portfolio Position

The Council's treasury debt portfolio position at 31st December 2010 comprised:

		Principal		Ave. rate
		£m		%
Fixed rate borrowing	PWLB	11.0		4.78
	Market	<u>15.9</u>	26.9	4.00
Variable rate borrowing	PWLB	0		
	Market	<u>0</u>		
Temporary Borrowing			8.0	0.56
TOTAL DEBT			<u>34.9m</u>	3.46
TOTAL INVESTMENTS			19.4m	3.06

5. Outlook for Interest Rates

- 5.1 The Bank of England cut interest rates to 0.5% in March 2009, its lowest level in its 315 year history as part of a continued effort to aid an economic recovery. It is expected that the Bank Rate will remain at this level for some time, and is not predicted to start to rise before the 2nd/ or 3rd quarter of 2011. Short – term money market rates will continue to pay at very low levels. This impact on investment income has been factored into 2011/12 investment budgets.

The recently announced Basel III capital/liquidity rules are positive for banks. However, the restructuring of UK bank balance sheets is ongoing and is expected to take a long time to complete, and is a pre-condition for eventual normalization of credit conditions and bank lending.

- 5.2 Part of the service offered by the Council's treasury advisers, Arlingclose Ltd, is to assist the Council to formulate a view on interest rates.

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The following table gives Arlingclose Ltd view:

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Official Bank Rate													
Upside risk	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	0.50	0.50	0.75	1.00	1.25	1.50	2.00	2.50	2.75	3.00	3.00	3.00	3.00
Downside risk	-	-	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50
1-yr LIBID													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	1.65	1.90	2.15	2.40	2.50	2.50	2.75	3.00	3.25	3.50	3.50	3.50	3.50
Downside risk	- 0.25	- 0.25	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50
5-yr gilt													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	2.75	3.00	3.25	3.50	3.75	4.00	4.00	4.00	4.00	4.00	4.25	4.25	4.00
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
10-yr gilt													
Upside risk	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	3.90	4.00	4.10	4.25	4.50	4.75	4.75	4.75	4.75	4.75	5.00	5.00	4.75
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
20-yr gilt													
Upside risk	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	4.50	4.75	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.25	5.25	5.00
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
50-yr gilt													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	4.25	4.50	4.75	4.75	4.75	4.75	4.50	4.50	4.50	4.50	4.75	4.75	4.50
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25

5.3 Outlook for the Economy

Credit - The availability of credit is still expected to remain restricted as banks address their balance sheets, particularly as banks change their lending behaviour and lower their lending risk. Also the uncertainty surrounding Eurozone sovereign debt will remain a driver of global credit market sentiment.

Growth – The path of base rates reflects the fragility of the recovery and the significantly greater fiscal tightening of the emergency budget. With growth and underlying inflation likely to remain subdued, the Bank of England will stick to its lower for longer stance on policy rates. Consumer Price Inflation (CPI) has risen to 3.7% driven largely by energy and transport prices and could peak at over 4% in the first quarter of 2011 with the impact of the VAT increase. CPI will remain high for the rest of the year and February's Inflation Report could be a key indicator to the timing and aggressiveness of interest rates.

Labour Market – employment outlook remains uncertain, as unemployment remains near a sixteen year high at just over 2.5 million as is set to increase as the Public Sector shrinks. Pay freezes and job losses will continue into 2011.

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6. Borrowing Strategy

The Council prefers to maintain maximum control over its borrowing activities as well as flexibility on its loan portfolio. A prudent and pragmatic approach to borrowing will be maintained to minimise borrowing costs without compromising longer-term stability of the portfolio, consistent with the Council's Prudential Indicators. In conjunction with advice from its treasury advisor, Arlingclose Ltd, the Chief Finance Officer will keep under review the options it has in borrowing from the PWLB, the market and other sources.

Any borrowing undertaken and the timing will depend on capital expenditure levels, interest rate forecasts and market conditions during the year in order to minimise borrowing costs. The Council will be advised by Arlingclose Ltd of the specific timing of borrowing. The overall borrowing must be within the Council's projected Capital Financing Requirement (CFR) and its approved Affordable Borrowing Limit.

7. Debt Rescheduling

The Council will continue to maintain a flexible policy for debt rescheduling. Market volatility may provide opportunities for rescheduling debt from time to time. The rationale for rescheduling would be one or more of the following:

- Savings in interest costs with minimal risk
- Balancing the ratio of fixed to variable debt
- Amending the profile of maturing debt to reduce inherent refinancing risks.

Any rescheduling activity will be undertaken following the rationale within the Council's Treasury Management Strategy. The Section 151 Officer will agree in advance with Arlingclose Ltd the strategy and framework within which debt will be repaid/rescheduled if opportunities arise. Thereafter the Council's debt portfolio will be monitored against equivalent interest rates and available refinancing options on a regular basis. As opportunities arise, they will be identified by Arlingclose Ltd and discussed with the Council's officers.

All rescheduling activity will comply with the accounting requirements of the local authority SORP and regulatory requirements of the Capital Finance and Accounting Regulations (SI 2007 No 573 as amended by SI 2008/414).

All rescheduling and any new long term borrowing undertaken will be reported to the Treasury Management Panel at the meeting following its action.

ANNUAL INVESTMENT STRATEGY

8. Investment Policy

The Council will have regard to the CLG's Guidance on Local Government Investments ("the Guidance") issued in March 2010 and CIPFA's Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities are:

- Security of the invested capital;
- Liquidity of the invested capital;
- An optimum yield which is commensurate with security and liquidity.

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As such it is important to restate the overall policy objective of the Annual Investment Strategy i.e. that:

‘the council should invest prudently the surplus funds held on behalf of the community giving priority to security and liquidity’.

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.

Investment instruments identified for use in the financial year are listed below under the ‘Specified’ Investments categories.

Specified investments are investments offering high security and high liquidity. The investments will be sterling denominated with maturities up to a revised maximum of 1 year and meet the minimum ‘high’ credit rating criteria where applicable.

SPECIFIED INVESTMENTS

All “Specified Investments” listed below must be sterling-denominated.

Investment	Max Sum per institution/group	Maximum period
Debt Management Agency Deposit Facility* (DMADF) <ul style="list-style-type: none"> this facility is at present available for investments up to 6 months 	NONE	6 months
Term deposits with the UK government or with UK local authorities (i.e. local authorities as defined under Section 23 of the 2003 Act) with maturities up to 1 year	£5m	1 year
Term deposits with credit-rated deposit takers (banks and building societies), including callable deposits, with maturities up to 1 year	£7m	1 year

Non-specified investments are of greater potential risk and cover deposit periods over one year. To protect against a lower for longer prolonged period of low interest rates and to provide certainty of income, two year deposits will be actively considered within the limits the Council has set for its specified and non-specified investments. Arlingclose Ltd, the council’s treasury advisors have been consulted with this change and have endorsed the extension of investments with UK Banks and Building Societies.

9. Lending criteria

Period of loans

On the advice of the treasury advisors Arlingclose Ltd and in view of the current prevailing interest rates, the council is seeking to extend lending to a maximum of 2 years and with only the institutions listed in the Councils approved lending list. There is one organisation which the Council could lend up to 3 years (Gloucestershire Airport Company), which the Council owns a 50% share in.

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Credit ratings

The credit crisis and exposure to Icelandic banks has focused attention on the treasury management priority of security of capital monies invested. An authorised 'Counter party lending' list is maintained by the treasury team on behalf of the Council's Section 151 Officer which includes those counterparties which meet the minimum criteria for lending. The Council will use Fitch, Moody's and Standard and Poor ratings to derive its criteria for lending. CIPFA suggests using the lowest rating from all three of the agencies to determine creditworthy counterparties, plus additional market information. On the advice of Arlingclose Ltd in order to minimise risk, the Council will restrict lending to those institutions which meet the following minimum criteria, defined as:

Moody's ratings:

Aaa – Aa3 are judged to be of the highest quality, with minimal credit risk for long term investments. The ratings from Aa may be modified by the addition of a 1, 2 or 3 to show relative standing within the category where the highest within the rating is 1 and 3 the lowest.

P-1 - Banks having this rating offer superior credit quality and a very strong capacity for timely payment of short-term deposit obligations.

Fitch ratings:

AAA - AA– Implies a bank with very high credit quality and denotes expectations of very low credit risk. They indicate very strong capacity for payment of long term financial commitments. The ratings may be modified by the addition of – or + where a + is higher rated within this category.

F1+ - Indicates the strongest capacity for timely payment of short term financial commitments.

S&P ratings:

AAA - AA– Implies a bank with very high credit quality and denotes expectations of very low credit risk. They indicate very strong capacity for payment of long term financial commitments. The ratings may be modified by the addition of – or + where a + is higher rated within this category.

A-1+ - Indicates the strongest capacity for timely payment of short term financial commitments.

The Council is alerted to changes in Fitch, Moody's and Standard & Poor's ratings through its treasury management advisors, Arlingclose Ltd. If a downgrade results in the counterparty/investment scheme no longer meeting the Council's minimum criteria, its further use as an investment will be withdrawn immediately. Likewise if a counterparty/investment scheme is upgraded and meets the lending criteria then it will be added to the 'counterparty lending list'.

The Council will monitor and update the credit standing of the institutions on a regular basis. It will not simply rely on credit ratings but will also consider alternative assessments of credit strength i.e. Statements of government support and information on corporate developments or market sentiment towards investment counterparties.

Size of deposits

In reviewing the lending criteria in view of the current market situation and based upon advice from Arlingclose Ltd the Council has restricted the lending list to a small number of very low risk counterparties. As such the following is recommended:

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The current authorised lending list meeting the criteria is as follows:

TABLE 3 CURRENT COUNTERPARTY LENDING LIST & LIMITS

BANKS	COUNTRY	LONG TERM			SHORT TERM			LIMIT £	TIME
		Fitch	Moody's	S&P	Fitch	Moody's	S&P		
Bank of Scotland (Lloyds Banking group)	GB	AA-	Aa3	A+	F1+	P-1	A-1	7,000,000	2 Years
Barclays Bank plc	GB	AA-	Aa3	AA-	F1+	P-1	A-1+	7,000,000	2 Years
Clydesdale Bank	GB	AA-	A1	A+	F1+	P-1	A-1+	7,000,000	1 Year
HSBC Bank plc	GB	AA	Aa2	AA	F1+	P-1	A-1+	7,000,000	2 Years
Lloyds TSB (Lloyds Banking Group)	GB	AA-	Aa3	A+	F1+	P-1	A-1	7,000,000	2 Years
Nat West Bank (RBS Group)	GB	AA-	Aa3	A+	F1+	P-1	A-1	7,000,000	2 Years
Royal Bank of Scotland (RBS Group)	GB	AA-	Aa3	A+	F1+	P-1	A-1	7,000,000	2 Years
Standard Chartered Bank	GB	AA-	A1	A+	F1+	P-1	A-1	7,000,000	1 Year
Santander UK PLC	GB	AA-	Aa3	AA	F1+	P-1	A-1+	4,000,000	6 months
BUILDING SOCIETIES	COUNTRY	LONG TERM			SHORT TERM			LIMIT £	TIME
		Fitch	Moody's	S&P	Fitch	Moody's	S&P		
Nationwide	GB	AA-	Aa3	A+	F1+	P-1	A-1	7,000,000	2 Years

GOVT & LOCAL GOVERNMENT	COUNTRY	LONG TERM			SHORT TERM			LIMIT £	TIME
		Fitch	Moody's	S&P	Fitch	Moody's	S&P		
Debt management account	GB	N/A	N/A	N/A	N/A	N/A	N/A	unlimited	6 Months
UK local authorities	GB	N/A	N/A	N/A	N/A	N/A	N/A	5,000,000	1 Year
Cheltenham Festivals	GB	N/A	N/A	N/A	N/A	N/A	N/A	100,000	1 Year

OTHER	COUNTRY	LONG TERM			SHORT TERM			LIMIT £	TIME
		Fitch	Moody's	S&P	Fitch	Moody's	S&P		
Gloucestershire Airport	GB	N/A	N/A	N/A	N/A	N/A	N/A	1,550,000	3 Years
Gloucestershire Everyman Theatre	GB	N/A	N/A	N/A	N/A	N/A	N/A	1,000,000	2 Years
Cheltenham Borough Homes	GB	N/A	N/A	N/A	N/A	N/A	N/A	5,000,000	2 Years

The Council's shorter term cash-flow investments are made with reference to the outlook for the UK Bank Rate and money markets. For these monies, the Council will mainly utilise its business reserve accounts, Government's Debt Management Office and Term deposits with UK Banks in 2011/12

The existing lending criteria, although limiting the exposure to individual institutions, does not limit the exposure to a particular country. The Icelandic bank position has raised the potential to do so.

TREASURY MANAGEMENT STRATEGY STATEMENT and ANNUAL INVESTMENT STRATEGY 2011/2012**10. Icelandic banks**

In early October 2008 all three of Iceland's major banks (Glitnir, Kaupthing and Landsbanki) collapsed following their difficulties in re-financing their short-term debt. In the UK, the Financial Services Authority (FSA) placed Kaupthing, Singer & Friedlander (the UK subsidiary of Kaupthing) into administration. The Council has logged claims for recovery of the deposits and some monies have been repaid in 2009 and 2010, leaving deposits of £9.41m still to be repaid. The likely recovery rates or timescales for future repayments is still unknown at this time.

11. Annual Minimum Revenue Provision (MRP) Statement

The annual MRP Statement is disclosed in Appendix 3.

12. Reform to the Council Housing Subsidy System

The government has confirmed its intention to scrap the HRA Subsidy System and replace it with a self financing alternative. Details of the new system will be announced following the recent Comprehensive Spending Review, and will be introduced in the Localism Bill later this autumn to enable the new system to start in 2012.

This will require the Council to fund the amount owed in the medium term through external borrowing or the use of internal resources. The Council will have the option to borrow from the PWLB or the market. The type of loans taken will be decided on in discussions with the Housing department and Arlingclose Ltd, the Council's treasury advisors.

13. Reporting on the Treasury Outturn

The Section 151 Officer will report to Council on its treasury management activities and performance against the strategy at least twice a year, one at mid year and a year end review at closedown time.

The Treasury Management Panel will be responsible for the scrutiny of treasury management activity and practices.

14. Other Items

In CIPFA's revised Code for Treasury Management, it requires the Section 151 Officer to ensure that all appropriate staff and members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Training requirements will be identified and any shortfalls will be met by Arlingclose Ltd or other organisations.