**TREASURY MANAGEMENT STRATEGY STATEMENT and ANNUAL INVESTMENT STRATEGY 2013/2014**

**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). 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 2013/14 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, Sector Treasury Services Limited. The strategy covers:

- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing requirement;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy;
- Annual MRP statement
- Policy on use of external service providers
- 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) 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 2013/14 to 2015/16

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".

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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'.

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. The Capital Prudential Indicators for 2013/14 – 2015/16

3.1.1 The Council's capital expenditure plans are the key driver of treasury management activity. The production of the capital expenditure plans are reflected in the prudential indicators, which are designed to assist members overview and confirm capital expenditure plans.

### 3.1.2. Capital expenditure

This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. Members are asked to approve the capital expenditure forecasts. It also summarises how these plans are being financed by capital or revenue resources. Any shortfall of resources will result in a borrowing requirement.

| **Capital Expenditure** | | | | | |
|---|---|---|---|---|---|
| Proposed Capital programme | 2011/12 £000 Actual | 2012/13 £000 Revised | 2013/14 £000 Estimate | 2014/15 £000 Estimate | 2015/16 £000 Estimate |
| General Fund | 7,094 | 8,943 | 4,236 | 1,097 | 1,332 |
| HRA | 4,740 | 5,492 | 6,472 | 5,662 | 8,864 |
| Total | **11,834** | **14,435** | **10,708** | **6,759** | **10,196** |
| **Financed by:** | | | | | |
| Capital receipts | 1,084 | 230 | 100 | 100 | 100 |
| Capital Grants | 1,388 | 1,527 | 366 | 306 | 306 |
| Capital Reserves | 4,640 | 6,485 | 6,677 | 5,437 | 6,395 |
| Revenue | 4,722 | 6,193 | 3,565 | 916 | 3,395 |
| **Net financing need for the year** | **11,834** | **14,435** | **10,708** | **6,759** | **10,196** |

### 3.1.3 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.

3.1.4 Estimates of the ratio of financing costs to net revenue stream for the current and future years, and the actual figures for 2011/12 are:

| **Ratio of Financing Costs to Net Revenue Stream** | | | | | |
|---|---|---|---|---|---|
| | 2011/12 Actual % | 2012/13 Revised % | 2013/14 Estimate % | 2014/15 Estimate % | 2015/16 Estimate % |
| Non-HRA | 5.05 | 3.36 | 3.51 | 3.30 | 3.25 |
| HRA | 2.66 | 8.92 | 8.39 | 8.13 | 7.87 |

3.1.5 **Capital Financing Requirement (CFR)**

The Capital Financing Requirement measures the authority's underlying need to borrow for a capital purpose. 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.

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

3.1.7 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 2012 are:

| **Capital Financing Requirement (CFR)** | | | | | |
|---|---|---|---|---|---|
| | 31/3/12 £000 Actual | 31/3/13 £000 Revised | 31/3/14 £000 Estimate | 31/3/15 £000 Estimate | 31/3/16 £000 Estimate |
| Non-HRA | 24,734 | 28,522 | 29,125 | 28,300 | 27,485 |
| HRA | 46,142 | 44,750 | 44,750 | 44,750 | 44,750 |
| Total CFR | 70,876 | 73,272 | 73,875 | 73,050 | 72,235 |

3.1.8 **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."

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

3.1.10 In order to ensure that over the medium term net borrowing will only be for capital purposes, the Council needs to ensure its gross 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 gross debt 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 | 2011/12 £000 Actual | 2012/13 £000 Revised | 2013/14 £000 Estimate | 2014/15 £000 Estimate | 2015/16 £000 Estimate |
|---|---|---|---|---|---|
| Gross borrowing | 72,472 | 69,077 | 69,044 | 68,972 | 66,660 |
| Capital financing requirement | 70,876 | 73,272 | 73,875 | 73,050 | 72,235 |
| Under/(Over) borrowing | (1,596) | 4,195 | 4,831 | 4,078 | 5,575 |

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

A fundamental indicator of the affordability of capital expenditure plans is its impact on council tax and housing rents. Any borrowing for capital purposes has an impact on the revenue account and, to the extent that 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 expenditure clearly has a direct impact on the revenue account and council tax/rents. The completed capital schemes will also have an impact in terms of running costs and income generation.

3.1.12 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.

3.1.13 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:

For the Band D Council Tax –

| 2013/14 | 2014/15 | 2015/16 |
|---|---|---|
| £Nil* | £Nil | £Nil |

* As a proposed Council Tax freeze for 2013/14.

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For average weekly housing rents

| 2013/14 | 2014/15 | 2015/16 |
|---|---|---|
| Nil** | Nil** | Nil** |

** Decisions on annual rent increases are subject to rent restructuring guidelines set by Central Government. As a consequence the Government has indicated that rent levels will increase annually by Retail Price Index plus 0.5% and this should cover all additional capital expenditure. This method has been used to form part of the 30 year HRA Business Plan.

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 Director of Resources (Designated 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** | | | | |
|---|---|---|---|---|
| | 2012/13<br>£000 | 2013/14<br>£000 | 2014/15<br>£000 | 2015/16<br>£000 |
| Borrowing | 109,000 | 109,800 | 110,670 | 111,600 |
| Other long term liabilities | - | - | - | - |
| Total | 109,000 | 109,800 | 110,670 | 111,600 |

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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 2013/14 to 2015/16 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 2013/14 is 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 Director of Resources (Designated 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** | | | | |
|---|---|---|---|---|
| | 2012/13 £000 | 2013/14 £000 | 2014/15 £000 | 2015/16 £'000 |
| Borrowing | 96,000 | 99,800 | 100,067 | 101,600 |
| Other long term liabilities | - | - | - | - |
| Total | 96,000 | 99,800 | 100,067 | 101,600 |

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 2012 was £72.472 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 2013/14, 2014/15 and 2015/16 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 2012/13, 2013/14 and 2014/15 of 100% of its gross outstanding borrowing.

3.3.4 This means the Director of Resources (Designated 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 2012 comprised:

| | | Principal £m | | Ave. rate % |
|---|---|---|---|---|
| Fixed rate borrowing | PWLB | 40.79 | | 3.83 |
| | Market | 15.90 | | 4.00 |
| | | | 56.69m | 3.88 |
| Variable rate borrowing | PWLB | 0 | | |
| | Market | 0 | | |
| Temporary Borrowing | | | 1.5m | 0.28 |
| **TOTAL DEBT** | | | **58.19m** | **3.79** |
| **TOTAL INVESTMENTS** | | | **9.95m** | **0.58** |

5. **Outlook for Interest Rates**

5.1 The Bank of England has now held interest rates at 0.5% since March 2009, its lowest level in its 317 year history as part of a continued effort to aid an economic recovery.

5.2 Part of the service offered by the Council's treasury advisers, Sector, is to assist the Council to formulate a view on interest rates. The Authority will reappraise its strategies from time to time in response to evolving economic, political and financial events.

The following table gives the Sector central view on future interest rates:

| | NOW | Dec-12 | Mar-13 | Jun-13 | Sep-13 | Dec-13 | Mar-14 | Jun-14 | Sep-14 | Dec-14 | Mar-15 | Jun-15 | Sep-15 | Dec-15 | Mar-16 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| BANK RATE | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.75 | 1.00 | 1.25 | 1.50 | 1.75 |
| 3 month LIBID | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.60 | 0.60 | 0.70 | 0.80 | 1.10 | 1.40 | 1.70 | 1.90 |
| 6 month LIBID | 0.70 | 0.70 | 0.70 | 0.70 | 0.70 | 0.70 | 0.70 | 0.80 | 0.90 | 1.00 | 1.10 | 1.30 | 1.60 | 1.90 | 2.20 |
| 12 month LIBID | 0.90 | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 | 1.10 | 1.10 | 1.20 | 1.30 | 1.30 | 1.50 | 1.80 | 2.10 | 2.40 |
| | | | | | | | | | | | | | | | |
| 5 yr PWLB | 1.60 | 1.50 | 1.50 | 1.50 | 1.60 | 1.60 | 1.70 | 1.70 | 1.80 | 2.00 | 2.20 | 2.30 | 2.50 | 2.70 | 2.90 |
| 10 yr PWLB | 2.50 | 2.50 | 2.50 | 2.50 | 2.60 | 2.60 | 2.70 | 2.70 | 2.80 | 3.00 | 3.20 | 3.30 | 3.50 | 3.70 | 3.90 |
| 25 yr PWLB | 3.80 | 3.70 | 3.80 | 3.80 | 3.80 | 3.80 | 3.90 | 3.90 | 4.00 | 4.10 | 4.30 | 4.40 | 4.60 | 4.80 | 5.00 |
| 50 yr PWLB | 3.90 | 3.90 | 4.00 | 4.00 | 4.00 | 4.00 | 4.10 | 4.10 | 4.20 | 4.30 | 4.50 | 4.60 | 4.80 | 5.00 | 5.20 |

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## 5.3 Outlook for the Economy

The economic recovery in the United Kingdom (UK) since 2008 has been the worst and slowest recovery in recent history. Growth prospects are weak and consumer spending, the usual driving force of recovery, is likely to remain under pressure due to consumers focusing on repayment of personal debt, inflation eroding disposable income, general malaise about the economy and employment fears.

This challenging and uncertain economic outlook has several key treasury management implications:

- The Eurozone sovereign debt difficulties provide a clear indication of high counterparty risk. This continues to suggest the use of higher quality counterparties for shorter time periods.

- Investment returns are likely to remain relatively low during 2013/14 and beyond.

- Borrowing interest rates continue to be attractive and may remain relatively low for some time. The timing of any borrowing will need to be monitored carefully.

- There will remain a cost of carry – any borrowing undertaken that results in an increase in investments will incur a revenue loss between borrowing costs and investment returns.

Economic forecasting remains difficult with so many external influences weighing on the UK. Sector believes that given the weak outlook for growth, the prospects for any changes in the Bank Rate before 2015 is very limited. There is potential for the start of Bank Rate increases to be even further delayed if growth disappoints.

## 6. Borrowing Strategy

6.1 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, Sector, the Director of Resources 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 Sector on 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. For 2013/14, the Council are looking to take out PWLB loans in respect of the Gloucestershire Airport Runway Safety Project (£1.2m) and for new build homes on garage sites on behalf of Cheltenham Borough Homes (£1.3m)

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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 Director of Resources (Designated Section 151 Officer) will agree in advance with Sector 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 Sector and discussed with the Council's treasury officers.

All rescheduling activity will comply with the accounting requirements of the local authority Code of Practice 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.

8. **Policy on borrowing in advance of need**

The council will not borrow more than or in advance of its need purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

9. **Sources of Borrowing**

9.1 In conjunction with advice from its treasury advisor, Sector, the Authority will keep under review the following borrowing sources:

- PWLB
- Local authorities (includes Police & Fire authorities)
- Commercial banks
- Money Markets
- Leasing

9.2 The cost of carry has resulted in an increased reliance upon shorter dated and variable rate borrowing. This type of borrowing injects volatility into the debt portfolio in terms of interest rate risk but is counterbalanced by its affordability and alignment of borrowing costs with investment returns. The Authority's exposure to shorter dated borrowing is kept under regular review and if margins change then the borrowing strategy could be maintained or altered.

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9.3 The Authority has £15.9 million exposure to LOBO loans (Lender's Option Borrower's Option) of which £7 million can be "called" within 2013/14. A LOBO can be called when the lender exercises its rights to amend the interest rate on the loan at which point the borrower can accept the revised terms or reject them and repay the loan. LOBO loans present a potential refinancing risk to the Council since the decision to call a LOBO is entirely at the lenders discretion. Any LOBO called will be discussed with the treasury advisers prior to acceptance of any revised terms.

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### 10. Investment Policy

The Council will have regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the 2011 revised CIPFA' 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.

Credit markets remain in a state of distress as a result of the excessive and poor performing debt within the financial markets and in some instances this has lead to a sovereign debt crisis (in countries such as Greece, Spain and Italy) with the outcome still largely unknown. It is against this backdrop of uncertainty that the Authority's investment strategy is framed.

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 heading.

**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.

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**SPECIFIED INVESTMENTS**
**All 'Specified Investments' listed below must be sterling-denominated.**

The types of investments that will be used by the Council

| Investment | Max Sum per institution/group | Maximum period |
|---|---|---|
| **Debt Management Agency Deposit Facility*** (DMADF)<br>• this facility is at present available for investments up to 6 months | UNLIMITED | 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 | £7m | 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 |
| **AAA rated Money Market Funds** with UK/Ireland/Luxembourg domiciled | £1m | 1 year |
| **T-Bills** issued by the DMO (Government) | UNLIMITED | 1 year |
| **Certificates of deposit (CD's)** issued by banks and building societies covered by UK Government (explicit) guarantee | £5m - £7m | 1 year |

**Non-specified investments** are of greater potential risk and cover deposit periods over one year. Sector continue to maintain the view that, for the time being, clients should look to the short end of the market when making investment decisions and it is the intention of this Council to lend for a maximum period of one year. The exception to this is the loan made to Gloucestershire Airport Company which the Council could lend up to three years. The Council does have a 50% share in the airport. If the money markets improve and following advise from Sector any extension of going beyond a year will need to be approved by Council.

11. **Lending criteria**

11.1 **Credit ratings**

In accordance with the above guidance from CLG and CIPFA, and in order to minimise the risk to investments, the Council has below clearly stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list. The creditworthiness methodology used to create the counterparty list fully accounts for the ratings, watches and the outlooks published by all three ratings agencies with a full understanding of these reflected in the eyes of each agency. Using the Sector ratings service potential counterparty ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications.

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Further, the Council's officers recognise that ratings should not be the sole reason of the quality of an institution. The assessment will also take account of information that reflects the opinion of the markets. The Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings. This is fully integrated into the credit methodology provided by the advisors, Sector in producing its colour codings which show the varying degrees of suggested creditworthiness. These colour codes are used by the Council to determine the recommended duration for investments. The Council will therefore use counterparties within the following durational brands

- Blue 1 year (only applies to nationalised or semi nationalised UK banks)
- Orange 1 year
- Red 6 months
- Green 3 months
- No colour Not to be used

Below is a brief terminology of the three credit rating agencies ratings:-

**Moody's ratings:**
Aaa – A3 are judged to be of the highest quality, with minimal credit risk for long term investments. The ratings 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 - A– 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 - A– 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.

All credit ratings will be monitored weekly as provided by Sector. If a down grade results in a change of colour for a financial institution, its further use as a new investment will be withdrawn immediately.

11.2 **Size of deposits**
In reviewing the lending criteria in view of the current market situation and based upon advice from Sector the Council has come up with a lending list for low risk counterparties within the UK. If the UK's sovereign rating is reduced, banks could still remain on the approved lending list, after taking advice from Sector. The list of counterparties which qualify are shown in Appendix 3. This list will be added to, or deducted from by officers should ratings change in accordance with this policy.

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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, Money Market Funds, Government's Debt Management Office (including T Bills), Term deposits with UK Banks and Certificate of Deposits (CD's) in 2013/14. The maximum duration for any deposit to be made to the above financial institutions is between one month and one year apart from those highlighted in the "other" category. These periods can be reduced or increased if the ratings of that institution are downgraded or upgraded. Treasury officers will take on board Sector's recommendations when it is received.

11.3 **Everyman Theatre**

The Gloucestershire Everyman Theatre approached the council in December 2012 with a request that the council consider supporting the cash flow for the theatre.

The refurbishment of the theatre, which is owned by the council, was funded by a £1m loan facilitated by the council from the Public Works Loans Board which the theatre will be paying off over the next 25 years plus £900k from the theatre's own reserves.

Following the closure in May to October 2011, the theatre did really well for 6 months to April 2012 exceeding financial projections. 2012/13 has seen a full year not affected by the closure but audiences have fallen consistently through the year leading to a projected loss. It is reasonable to say that the cause is the current economic climate and level of public confidence.

The theatre has taken steps to address their trading position. Significant staff savings have been made, various cut backs and also changes to the contractual arrangements with producers to lessen the profit required from the theatre performances. Financial projections have been considered by both the council members for Finance and Sport and Culture in consultation with the Section 151 Officer and provide some comfort that the borrowing would be short term. As such, it is recommended that members support a request for a £100,000 borrowing facility, included within the "other" category on the counterparty lending list.

11.4 **Council's Banker**

The Council banks with LloydsTSB (Lloyds Banking Group). On adoption of this Strategy, it will meet the minimum credit criteria of A- (or equivalent) long term. It is the Councils intention that even if the credit rating of LloydsTSB falls below the minimum criteria A- the bank will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

11.5 **Money Market Funds (MMFs)**

Money Market Funds will be utilised but good treasury management practice prevails, and whilst MMFs provide good diversification the Council will also seek to diversify any exposure by utilising more than one MMF. Currently the Council has no MMF's but they have been recommended to us by Sector as another investment tool.

12. **Annual Minimum Revenue Provision (MRP) Statement**

The annual MRP Statement is disclosed in Appendix 4.

13. **Balanced Budget Requirement**

The Authority complies with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

14. **Reporting on the Treasury Outturn**

**TREASURY MANAGEMENT STRATEGY STATEMENT and ANNUAL INVESTMENT STRATEGY 2013/2014**

The Director of Resources, (Designated 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.

15. **Other Items**

15.1 **Training**
In CIPFA's Code for Treasury Management, it requires the Director of Resources (Designated 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 Sector or other organisations.

15.2 **Treasury Advisors**
The CLG's Guidance on local government investments recommend that the Investment Strategy should state:

- Whether and, if so, how the authority uses external advisors offering information, advice or assistance relating to investment and
- How the quality of any such service is controlled.

15.3 The Council appointed Sector Treasury Services Ltd as its external advisor in December 2012. They can provide us with information, advice and assistance in all areas of treasury. The Council aims to have a close working relationship with Sector and will be in contact with their advisors on a regular basis (weekly) and daily if necessary. A detailed schedule of services is listed within the contract. The Council recognises that responsibility for treasury management decisions remains with the Council at all times.