TREASURY STRATEGY STATEMENT FOR 2012/13

1 Introduction

1.1 This Treasury Strategy Statement details the expected activities of the Treasury function in the next financial year (2012/13). Its production and submission is a requirement of the Council's Treasury Management Policy. Its format and structure is as required by the Policy. The strategy covers:

- The current portfolio position
- Treasury limits in force which will limit the treasury risk and activities of the Council
- The borrowing strategy
- The investment strategy
- The extent of debt rescheduling opportunities
- Any extraordinary treasury issues

2 Current Portfolio Position

2.1 Loans Outstanding as at 31/12/12

	Amount £	Average Interest Rate %	Cumulative Rate %
Public Works Loans Board Loans	1,964,982	8.25	8.86
Lender Option Borrower Option Loans	1,000,000	10.13	10.10
	2,964,982	8.88	8.53

2.2 Investments as at 31/12/12

	Amount £	Average Interest Rate %
Barclays Bank	2,500,000	2.50
Co-op Bank	3,060,000	0.86
Cumberland Bldg Soc	1,000,000	2.05
Furness Bldg Soc	4,000,000	2.53
Hinckley & Rugby Bldg Soc	2,000,000	1.71
HSBC	375,000	0.25
Ipswich Bldg Soc	1,500,000	2.90
Manchester Bldg Soc	3,000,000	2.33
Market Harborough Bldg Soc	3,000,000	2.29
Marsden Bldg Soc	2,500,000	2.66
Melton Mowbray	4,000,000	2.04
Nat West Bank	7,000,000	0.90
National Counties Bldg Soc	3,500,000	2.80
Newbury Bldg Soc	2,000,000	3.00
Nottingham Bldg Soc	4,750,000	1.88
Principality Bldg Soc	4,250,000	3.01
Progressive Bldg Soc	2,000,000	3.08
Royal Bank of Scotland	2,750,000	1.75
Scottish Bldg Soc	2,000,000	2.25
Skipton Bldg Soc	2,250,000	1.71
	57,435,000	2.41

3 Treasury Limits for 2012/13

3.1 Under the Prudential Code for Capital Finance in Local Authorities, the Council is required to set indicators for each financial year:-

3.1.1 CIPFA Code of Practice for Treasury Management in the Public Service
3.1.2 Interest Rate Exposure
3.1.3 Maturity Structure of Borrowing
3.1.4 Total Principal Sums Invested for Periods Longer than 364 Days
3.1.5 Estimates of Ratio of Financing Costs to Net Revenue Stream
3.1.6 Estimate of the incremental Impact of Capital Investment decisions on the Council Tax
3.1.7 Net Borrowing and the Capital Financing Requirement
3.1.8 Estimates of Capital Financing Requirement

3.2 The above decisions must be made by the full Council before the beginning of the financial year to which the decisions relate, though the decisions can subsequently be varied at any time, any variation must likewise be determined by the full Council.

3.3 CIPFA Code of Practice for Treasury Management in the Public Service

3.3.1 The CIPFA Code of Practice on Treasury Management in Local Authorities was re-approved by Cabinet on 3rd February 2003. The Code of Practice on Treasury Management is adopted every year as part of the Treasury Management Strategy.

3.4 Interest Rate Exposure

3.4.1 Under the Prudential Code for Capital Finance, Authorities are required to set for the forthcoming financial year and the following two years upper limits to its exposure to the effects of changes in interest rates. These prudential indicators will relate to both fixed interest rates and variable interest rates and will be referred to as upper limits on fixed and variable interest rate exposure.

3.4.2 The upper limits on fixed and variable interest rate exposures may be expressed either as absolute amounts or as percentages. They may be related either to the Authority's net interest or net principal amounts outstanding on its borrowing / investments.

3.4.3 Effective ranges within which interest exposure will be managed:
Fixed rates – either 70% to 100% or

2012/13	£27.0Mcr to £38.6Mcr
2013/14	£26.1Mcr to £37.3Mcr
2014/15	£27.6Mcr to £39.4Mcr

Variable rates – either 0% to 30% or

2012/13	£0.M to £11.6Mcr
2013/14	£0.M to £11.2Mcr
2014/15	£0.M to £11.8Mcr

3.4.4 The effective ranges within which interest rate exposure have been calculated are based on the projected outstanding balances shown in the table below.

		2012/13	2013/14	2014/15
		£	£	£
Total Projected Principal Outstanding on Borrowing		6,892,013	6,264,844	5,659,444
Total Projected Principal Outstanding on Investments		(45,485,397)	(43,515,365)	(45,059,870)
Net Principal Outstanding		(38,593,384)	(37,250,521)	(39,400,426)
Upper Limit – Fixed Rates = 100%	or	(38,593,384)	(37,250,521)	(39,400,426)
Upper Limit – Variable Rates = 30%	or	(11,578,015)	(11,175,156)	(11,820,128)

3.5 Maturity Structure of Borrowing

3.5.1 Under the Prudential Code for Capital Finance, Authorities are required to set for the forthcoming financial year both upper and lower limits with respect to the maturity structure of its borrowing. The prudential indicators for the upper and lower limits are calculated on projected borrowing that is fixed rate, maturing in each period, expressed as a percentage of the total projected borrowing that is fixed.

3.5.2 This indicator is designed to be a control over having large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates.

3.5.3 The table below shows the upper and lower limits with respect to the maturity structure of borrowing. At any point in time, the actual percentages of debt projected to mature in each year will add up to 100%. However, the proposed indicator is for a range of approved percentages, and this gives discretion to act within that range. Therefore, the upper and lower limits need not add up to 100%.

	Actual 2011/12	Upper Limit 2012/13	Lower Limit 2012/13
Under 12 Months	5%	30%	21%
12 Months and within 24 Months	21%	25%	21%
24 Months and within 5 Years	57%	60%	41%
5 Years and within 9 Years	4%	20%	15%
9 Years and above	13%	10%	2%

3.6 Total Principal Sums Invested for Periods Longer than 364 Days

3.6.1 To maximise investment interest and take advantage of higher long term interest rates, Cash Managers will continue to be permitted to invest for longer than 364 days. A maximum of £20M in total may be invested longer than 364 days with a maximum term of 5 years. All decisions made on long term investments will be made in conjunction with Officers and will be dependant on market conditions and cashflow. Deals longer than two years will require approval by the S151 Officer.

3.6.2 An indication of longer term rates is shown below. The average rate achieved by the Cash managers to date is 2.60% for Sterling and 2.26% for Tradition.

Term	Int. Rate 05/01/12	Interest Generated in year on £1M
1 Year	1.70	17,000
2 Year	2.95	29,500
3 Year	3.40	34,000
4 Year	3.45	34,500
5 Year	3.60	36,000

3.6.3 To ensure liquidity of funds to meet cash flow requirements, in House investments will not be made for periods longer than 364 days.

4 Borrowing Strategy 2012/13

4.1 The New Prudential Code, under the Local Government Act 2003, requires Local Authorities to set an Authorised limit and an operational boundary for its total external debt. This replaces part IV of the Local Government and Housing Act 1989, which required Local Authorities to set the overall borrowing limit, the short term borrowing limit and the proportion of interest which is payable by them at variable rates.

4.2 The Authorised Limit should reflect a level of borrowing which could be afforded but may not be sustainable. It is set to establish the outer boundary of the Authority's borrowing.

4.3 The Operational Boundary focuses on the day to day treasury management activity. It is a means by which the Authority manages its external debt to ensure that it remains within the Authorised Limit.

4.4 The table below shows the Authorised Limits and the Operational Boundaries for the forthcoming year and the following two years.

	2012/13	2013/14	2014/15
	£	£	£
Operational Boundary	8,000,000	8,000,000	8,000,000
Authorised Limit	10,000,000	10,000,000	10,000,000

4.5 Standard policy in the past has been to not take out new borrowing but to utilise capital receipts' set aside reserves. However, borrowing will be required in 2012/13 to fund capital projects. Borrowing would only be considered for a particular capital scheme.

4.6 The table below details capital spend and how the capital programme will be funded.

	2012/13	2013/14	2014/15
	£	£	£
Capital Programme	**5,232,590**	**4,283,000**	**1,385,000**
Funded By:			
Capital Contribution	96,700	1,240,000	0
Capital Receipt	2,655,560	2,313,000	1,130,000
Government Grant	753,000	470,000	255,000
Prudential Borrowing	1,727,330	260,000	0
Revenue Contribution	0	0	0
Total Funding	**5,232,590**	**4,283,000**	**1,385,000**

4.7 The table below is an indication of the current borrowing rates available and shows the likely impact on the General Fund and the incremental Impact of Capital Investment on Council Tax.

Amount	Period	PWLB Interest Rate 04/01/12 %	Interest Payable pa £	Equivalent increase in Council Tax
£1M	1 Year	1.25	12,500	0.13%
£3M	1 Year	1.25	37,500	0.38%
£5M	1 Year	1.25	62,500	0.63%
£1M	2 Years	2.05	20,500	0.21%
£3M	2 Years	2.05	61,500	0.62%
£5M	2 Years	2.05	102,500	1.03%

4.8 The table below shows the ratio of financing costs to net revenue stream. The ratio will decrease in 2010/11 due to a reduction in capital charges in the General Fund but will increase in future years as the capital charges in the General Fund increase.

2010/11 Actual	2011/12 Est	2012/13 Est	2013/14Est	2014/15 Est
16.36%	11.89%	23.10%	23.50%	23.94%

4.9 The Capital Financing Requirement (CFR) as at the 1st of April 2012 is estimated to be a negative £36.93M. Where the CFR is nil or negative on the last day of the financial year, this indicates that the Authority’s provision for debt is equal to or greater than the debt incurred. There is accordingly no need to make a Minimum Revenue Provision in the following year. Without a significant increase in the amount of borrowing it is estimated the Capital Financing Requirement will remain negative during 2013/14 and 2014/15. The capital financing requirement of a local authority will increase whenever capital expenditure is incurred and not resourced immediately (from useable capital receipts, direct charge to revenue or capital grant) and represents an increase in the underlying need to borrow for a capital purpose. This will be the case whether or not external borrowing actually occurs.

4.10 The Profile of External debt at 31/03/12

	P.W.L.B. **£(000)**	Banks etc. **£(000)**	Other **£(000)**	Total **£(000)**
Maturing in 2012/13	627		-	627
Maturing in more than 1 and less than 2 years	606	-	-	606
Maturing in more than 2 and less than 5 years	179	1,000	-	1,179
Maturing in more than 5	480	-	-	480
	1,892	1,000	-	2,892

4.11 External debt of £627K will be repaid during 2012/13. This comprises of installment repayments and loans that are maturing during the year. This is more than the current year’s payment of £152K, because of an increase in the repayment of PWLB.

4.12 The premiums for premature repayment on PWLB is extremely expensive and not cost effective to repay debt early. Should rates change, the situation will be reviewed.

5 Investment Strategy 2012/13

5.1 As Members are aware, since 1990 the Council was required to 'set aside' a proportion of every capital receipt for debt repayment. Although the Council is now a substantial net lender of money, the impact of 'set aside' has been to dramatically reduce external debt while increasing our credit position on the credit ceiling.

5.2 Because the Council has been generating 'set aside' capital receipts at a much faster rate than new borrowing allocations, treasury management policies have been geared to net debt reduction over time. As a lender will normally receive less interest than a borrower will pay (and also because of very tight government imposed investment rules), the Council has sought to consistently minimise external debt rather than lend surplus funds out.

5.3 'Set aside' monies have been internally invested rather than formally used to repay debt. The 2003 Local Government Act changed the requirements to set-aside receipts from Housing Stock transfers and Officers are currently investigating the options to use the set-aside receipts.

5.4 Outstanding debt relates predominantly to old Housing activities. All current outstanding loans have been arranged at effectively fixed rates and are immune from day to day variations in general interest rates.

5.5 External debt at 31/12/11 was £3.0M compared to investments of £57.4M. The Interest received on investments is expected to be in the region of £1.1M for the year compared to interest paid on loans of £0.27M.

5.6 The balance of outstanding investments at the 31st March 2012 is expected to be in the region of £46M.

5.7 It is proposed that the current arrangements whereby investments are split between two External Cash managers and In-House continue. The maximum levels for 2012/13 are as follows:

External Cash Manager	£23 Million
External Cash Manager	£23 Million
Managed In House	£22 Million

5.8 The value managed In House, maximum limit of £22M, will be used to control daily cash flow and monitor internal performance with the Cash managers. The levels of funds split between the Cash managers and In House will be monitored throughout the year to ensure there are sufficient funds maintained In House to meet all cash flow requirements. If funds are required, the level placed with the Cash managers will be reduced and managed In House.

5.9 The policy of splitting investments between two external cash managers enables the Authority to continue to monitor performance and seek to attain best value. Reports are presented to Cabinet as part of the quarterly monitoring process showing the activity of the external cash managers.

5.10 The table below specifies counterparties with whom investments can be made and the limits on investments with those organizations. There has been no change to the 2011/12 limits.

5.11 In light of the collapse of the Icelandic banks, NHDC will continue the policy to not invest any funds in non UK Banks. There has in the past been the ability to lend to non UK banks but this has never been used. From recent experiences the UK Government has been willing to assist troubled institutions in the UK and as such, the amount of risk to the Council of investing in UK Banks is considered less than investing in non UK Banks. NHDC will only lend to UK banks with a credit rating for longer term deals greater than "BBB" and F3 or above for short term credit ratings. (These are Fitch definitions of ratings).

	Total Maximum Amount of Investment			
	£9 Million	**£9 Million**	**£6 Million**	**£4 Million**
UK Clearing Banks with a credit rating greater than BBB	All			
UK Clearing Banks – Wholly owned Subsidiaries with a credit rating greater than BBB		All		
Discount Houses (Guaranteed by Bank of England)		All		
Building Societies	Assets £4.5bn	Assets £2.5bn to £4.5bn	Assets £1bn to £2.5bn	Assets £0.3bn- £1bn
Public Corporations	All			
Other Local Authorities	All			

5.12 In conjunction with the limits set out above, credit ratings will be used where available in deciding who to lend to. This practice has been in place since its recommendation in the Treasury Management Audit report in Feb 2009 where ratings have been obtained from Fitch. The limitation of credit ratings is acknowledged and investment decisions will be based on a combination of asset size, credit rating and information obtained from other sources such as the financial press.

5.13 Not all building societies are credit rated but this will not preclude them from the lending list if they fulfill the criteria above.(Building societies have to pay the credit rating agency to obtain a rating). Where a society does have a rating, this will be considered at the time of the deal taking into account the amount of investment and the length of the deal.

5.14 As well as imposing maximum limits with each counter party, the overall percentage of outstanding investments with each counterparty will be assessed to ensure a reasonable spread of investments.

5.15 The counter party list will be monitored and updated to take account of mergers and takeovers of institutions which might impact on the spread of investments.

5.16 In line with the 2011/12 policy, the maximum time for any one investment made in house is limited to a period not exceeding 364 days. Continuing the policy of 2011/12, Cash Managers will still be permitted to invest longer than 364 days. A maximum of £20M in total may be invested longer than 364 days with a maximum term of 5 years. This will enable the Cash Managers to take advantage of an increase in longer term rates should they increase during the year. Discretion will be applied to deals longer than 364 days and will only be entered into with NHDC officer approval. Deals longer than two years will require approval by the S151 Officer. To enable the Council to take advantage of preferential interest rates when they arise, it is recommended that forward deals continue to be entered into. Forward dealing rates will be monitored and this process will be reviewed during the year.

5.17 Due diligence will be given to investments to ensure the underlying Treasury principal of Security, Liquidity, Yield. There have been instances when a lower rate of interest has been taken in order to maintain the spread of investments. There has also been an instance where a lower rate of interest was taken due to the weighting of the credit risk exposure of the suggested counterparty.

5.18 The estimated investment interest for 2012/13 is approximately £1.1M. This has been calculated using an average of 2.0% for new deals made during the year for the Cash Managers and 0.87% in house.

5.19 Currently interest rates are low and it is prudent to invest surplus funds for short terms. Should interest rates rise investment interest can be maximised by reinvesting at a higher rate. Cash managers will advise on terms and market changes.

6 Debt Rescheduling

6.1 Any debt rescheduling is likely to take place when fixed interest rates are anticipated to be at their highest, although the situation will be continually monitored in order to take advantage of any perceived anomalies in the yield curve. This will be reviewed as part of the Treasury Management action plan as part of debt free analysis.

7 Extraordinary Issues

7.1 The possibility of investing in Money Market Funds may be investigated during the year if the level of interest generated from such investments proves worthwhile and it can be demonstrated that the level of risk can be maintained within levels defined in this statement.