Appendices

Item No.

NORTHAMPTON
BOROUGH COUNCIL

CABINET REPORT

Report Title	TREASURY STRATEGY 2008-09 TO 2010-11

AGENDA STATUS: **PUBLIC**

Cabinet Meeting Date:	20 February 2008
Key Decision:	YES
Listed on Forward Plan:	YES
Within Policy:	YES
Policy Document:	YES
Directorate:	Governance and Improvement
Accountable Cabinet Member:	Malcolm Mildren
Ward(s)	Not Applicable

1. Purpose

1.1 The purpose of the report is to:

a) Bring to Cabinet and Council the proposed Treasury Strategy for 2008-09 to 2010-11.

b) In the context of (a) above, to inform Cabinet and Council of the treasury issues to be considered over that timeframe.

2. Recommendations

2.1 That the Council be recommended to approve the Treasury Strategy for 2008-09 to 2010-11, incorporating:

a) The Capital Financing and Borrowing Strategy for 2008-09 to 2010-11 (paragraphs 3.2.1 to 3.2.6) as required by the Council's Treasury Management Policy Statement (TMP6 Reporting Requirements and Management Information Arrangements), and including:

(i) The Council's policy on the making of Minimum Revenue Provision (MRP) for the repayment of debt, as required by the Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008.

(ii) The Affordable Borrowing Limit for 2008-09 to 2010-11 as required by the Local Government Act 2003.

b) The Investments Strategy for 2008-09 to 2010-11 (paragraphs 3.2.7 to 3.2.11) as required by the DCLG (formerly ODPM) Guidance on Local Government Investments issued in 2004.

2.2 That the Cabinet note:

a) The measures being taken to manage the sensitivity of the forecasts (paragraph 3.2.12).

b) The proposed Debt Financing Budget 2008-09 to 2010-11 (Annex A and paragraph 3.2.13).

c) Adherence to the Council's policy on reserves and balances (paragraph 3.2.14).

d) Compliance with the requirement under the Local Government Act 2003 to produce a balanced budget (paragraph 3.2.15).

e) The forthcoming review of the Council's Treasury Management Practices (TMPs) (paragraph 3.2.16).

3. Issues and Choices

3.1 Report Background

3.1.1 The Council has to consider its annual Treasury Strategy under the requirements of the CIPFA Code of Practice on Treasury Management. The Council adopted the code of practice following its publication in 2001; this was formally minuted as a decision at the Council meeting of 21 January 2008

3.1.2 The CIPFA Prudential Code for Capital Finance in Local Authorities, published in October 2003, introduced enhanced requirements for the manner in which capital spending plans are to be considered and approved, and in conjunction with this, the requirement for an integrated treasury management strategy.

3.1.3 The Prudential Code requires the Council to set a number of prudential indicators for capital finance and a report setting out the prudential indicators for 2008-09 to 2010-11 is included elsewhere on this agenda. This report includes those prudential indicators to which regard should be given when determining the Council's Treasury Management Strategy for the next three financial years.

3.1.4 The Council's Treasury Management Strategy is made up of the following:

- The Capital Financing and Borrowing Strategy; and
- The Investments Strategy.

3.2 Issues

Capital Financing and Borrowing Strategy

3.2.1 The Capital Financing and Borrowing Strategy covers:

- Capital financing (3.2.2)
- New borrowing (3.2.3)
- Interest rate exposure (3.2.4)
- Prudential indicators (3.2.5)
- Temporary borrowing (3.2.6)

3.2.2 Capital Financing

a) The capital programme is financed mainly by sources other than borrowing, including capital receipts, grants, third party contributions and revenue contributions. However borrowing may be used where government award borrowing approvals in the form of Supported Capital Expenditure (Revenue) (SCE(R)) and provide associated revenue support, or when other financing sources are not available, in which instance prudential borrowing may be undertaken.

b) The Council makes limited use of operating leases to fund some types of expenditure that would otherwise be treated as capital. This policy is currently under review, and where operating leases offer better value for money these will now be considered as a financing source in place of capital outlay. Examples of the types of expenditure that might be suitable are IT equipment and office furniture. The annual costs of operating leases are treated as revenue expenditure in the accounts and are not included in the Council's capital programme.

   The Council's policy is not to enter into finance leases, which have to be treated as capital expenditure in the accounts, and generally do not offer any financial benefits to the authority.

c) Existing borrowing to fund capital expenditure in previous years stands at £26.6m. This borrowing is primarily in the form of Money Market LOBO (Lenders Option, Borrowers Option) loans.

d) Previously the Council has been required by statute to repay a minimum amount of 4% of debt principal each year. This debt repayment is known as the Minimum Revenue Provision (MRP).

   The Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008, which are due to come into force on or before 31st March 2008, now require local authorities to make instead 'prudent provision' for the repayment of debt. A number of options for prudent provision are set out in the regulations. The underlying principle is that the repayment of debt should be more closely aligned to the useful life of the asset or assets for which the borrowing has been carried out.

   As a transitional measure, authorities will be able to calculate MRP for all capital expenditure prior to 1 April 2008 as if the previous regulations were still in force.

   The authority is required, under the new regulations, to prepare an annual statement of their policy on making MRP for submission to Council.

   The Council's policy is to use the transitional arrangements to continue to provide for MRP under existing regulations pending the development of a more detailed policy following the publication of the regulations (which are currently still only available in draft form). The detailed policy will be brought to Council for consideration in 2008-09.

   For the next 3 years MRP, calculated under existing regulations, is estimated at:

	2008-09 £m	2009-10 £m	2010-11 £m
Repayment of debt principal (MRP)	0.54	0.64	0.64

   These figures incorporate the ongoing revenue impact of the new borrowing set out at paragraph 3.2.3 below.

3.2.3 New Borrowing

a) Under the Local Government Act 2003 local authorities are able to borrow in year for the current year capital programme and for the following two years. It is estimated that the new borrowing required to fund the 2008-09 capital programme will be £3.5m (gross of MRP).

b) The Council currently has no plans to undertake further prudential borrowing in 2009-10 and 2010-11. The new long-term borrowing requirement for the next three years is estimated at:

		2008-09 **£m**	**2009-10** **£m**	**2010-11** **£m**
(i)	New borrowing to cover new capital expenditure	3.50	0.00	0.00
(ii)	Replacement of loans maturing in year	0.00	0.00	0.00
(iii)	Less: debt repayment (see paragraph 3.2.2(d) above)	(0.54)	(0.64)	(0.64)
	Total new borrowing/(provision for debt repayment)	**2.96**	**(0.64)**	**(0.64)**

c) The Council is entitled to use Public Works Loan Board (PWLB) loans for its long term borrowing needs. In addition loans, including LOBO loans, are available from major banks via the Money Market and these may be considered when they offer better value than PWLB loans. Decisions on the timing and type of the borrowing will be taken in consultation with the Council's treasury advisors, Sector Treasury Services.

d) **Annex A** shows the maturity profile of existing debt, and the debt profile by interest rates. As is the current practice, the debt portfolio will be kept under review throughout 2008-09 and beyond; with debt rescheduling opportunities being investigated for potential interest savings. Recent changes to regulations, and to the structure of PWLB rates mean that rescheduling opportunities are more limited than in the past, but decisions will be based on appropriate advice and the maturity profile of the portfolio.

e) The Council also has a £1m overdraft facility with its bankers, the Co-operative Bank. This is only used on rare occasions to cover unforeseen events. Interest is charged at 1% above base rate for the use of this facility.

3.2.4 Interest Rate Exposure

a) Long Term Rates – Interest rates on PWLB and Money Market loans fluctuate daily according to market conditions, related in particular to the position on the gilt market.

The table below illustrates the prevailing PWLB rates and forecasts to March 2010, as at 1st February 2008.

Long Term Borrowing Rates - PWLB Maturity Loan Interest Rates			
	10 Years	**25 Years**	**50 Years**
2007-08			
Actual at 1 February 2008	4.63%	4.54%	4.45%
2008-09			
Forecast Quarter 1	4.60%	4.55%	4.50%
Forecast Quarter 2	4.55%	4.50%	4.45%
Forecast Quarter 3	4.50%	4.50%	4.50%
Forecast Quarter 4	4.50%	4.50%	4.50%
2009-10			
Forecast Quarter 1	4.55%	4.50%	4.45%
Forecast Quarter 2	4.55%	4.55%	4.50%
Forecast Quarter 3	4.65%	4.60%	4.55%
Forecast Quarter 4	4.70%	4.65%	4.60%

LOBO rates on offer for 70-year loans at 1 February 2008 were at 4.25% and below, dependant on the initial fixed period of the loan.

The Council's Borrowing Strategy for 2007-08 will be to use fixed rate borrowing where long-term rates are favourable. Where variable rate borrowing is used, short-term loans will be arranged in order that they can be replaced by long-term fixed rate loans at a later date when rates are more favourable.

b) Short-term rates – The bank base rate commenced this current year 2007/08 at 5.25% but due to fears of high inflation and other spending indicators the Bank of England increased the rate throughout the year to its highest level of 5.75%. This was reduced on 13th Dec to 5.50%, and again on 7th February to its present level of 5.25%.

The current forecasts indicate that the base rate will be further reduced during 2008 but there appears to be some difference of opinion as to how much and when this will occur. However Sector, our Treasury Advisors, forecast a base rate fall to 5.00% in June 2008 and a further reduction to 4.75% in Sept 2008. It is forecast that this rate will continue into 2009 and possibly as far as 2011. The table below illustrates the actual and forecast bank base rates for 2007-08 and 2008-09.

	Base Rate
2007-08	
Actual at 1 April 07	5.25%
Actual at 10 May 07*	5.50%
Actual at 12 July 07*	5.75%
Actual at 13 Dec 07*	5.50%
Actual at 7 Feb 08*	5.25%
Forecast at 31 March 08	5.25%
2008-09	
Forecast Quarter 1	5.25%
Forecast Quarter 2	5.00%
Forecast Quarter 3	4.75%
Forecast Quarter 4	4.75%
2009-10	
Forecast Quarter 1	4.75%
Forecast Quarter 2	4.75%
Forecast Quarter 3	4.75%
Forecast Quarter 4	5.00%

* Date of Rate Change

3.2.5 Prudential indicators

The prudential indicators that relate to the Capital Financing and Borrowing Strategy are reproduced at **Annex B**. These are:

a) Authorised limit for external debt for 2007-08, 2008-09, 2009-10 and 2010-11.

b) Operational boundary for external debt for 2007-08, 2008-09, 2009-10 and 2010-11.

c) Maturity structure of borrowing.

The Local Government Act 2003 requires the authority to set an Affordable Borrowing Limit. This is equivalent to the authorised limit at paragraph 3.2.5(a) above.

Affordable Borrowing Limit			
2007-08 Limit £000	2008-09 Limit £000	2009-10 Limit £000	2010-11 Limit £000
47,000	43,000	43,000	43,000

As indicated above (paragraph 3.2.3(a)) current accounting rules allow local authorities to forward funding for their capital programmes up to a maximum of three years. The affordable borrowing limit figures include a provision for future forward funding should it be advantageous to do so.

Cabinet are asked to recommend to Council that they approve the Affordable Borrowing Limits for 2008-09 to 2010-11.

3.2.6 Temporary Borrowing

The Council occasionally undertakes short term temporary borrowing to cover its cash flow position.

In addition the Council manages deposits from a small number of local organisations – Orchestras Live (Eastern Orchestra Board), Northampton Volunteer Bureau, and Billing Parish Council. (Orchestras Live have given notice that they are to cease this arrangement with effect from 31 March 2008.) No formal agreements have been set up with these organisations, and interest rates have traditionally been set on a custom and practice basis, with reference to the prevailing bank rate. Officers will shortly take action to set up formal agreements with these organisations, incorporating a defined method of calculating the interest rate to be applied.

Investments Strategy

3.2.7 The Investments Strategy covers:

- Investments (3.2.8)
- Liquidity of Investments (3.2.9)
- Interest Rates (3.2.10)
- Prudential indicators (3.2.11)

3.2.8 Investments

a) Under the Local Government Act 2003 the Council is required to have regard to the DCLG (formerly ODPM) Guidance on Local Government Investments issued in March 2004 and CIPFA's Treasury Management in the Public Services Code of Practice (2001) and updated Guidance Notes (2006).

b) The DCLG Guidance on Local Government Investments requires that investments are split into two categories:

(i) Specified investments – broadly, sterling investments, not exceeding 364 days and with a high credit rating.

(ii) Non-specified investments – do not satisfy the conditions for specified investments.

The detailed conditions attached to each of these categories are set out in **Annex C.**

All investments, with the exception of those to other local authorities, will be placed only with those banks, building societies and authorised deposit takers under the Financial Services and Markets Act 2000 and allocated a satisfactory colour rating by Sector Treasury Services, whose list is updated monthly. This list is based upon credit ratings issued by the three main rating agencies. Any changes to ratings during the month are notified to the authority immediately and action taken to remove from/add to the list as appropriate.

c) Specified Investments

The majority of the Council's investments in 2008-09 will fall into the category of specified investments.

d) Non-Specified Investments

Prior to the start of each financial year officers will review which categories of non-specified investments they consider could be prudently used in the coming year.

The officer recommendation for 2008-09 is that long-term investments (those for periods exceeding 364 days) could prudently be used where interest rates are favourable and funds are not required for short-term cashflow management.

The maximum amount that the Council will hold at any time during the year as long-term investments is £5m. This is within 10% of the forecast average level of total investments in 2008-09, which is around £58m. This could be undertaken without having an adverse effect on cashflow (see paragraph 3.2.9(a) below).

Advice will be taken from Sector Treasury Services before entering into any long-term investments.

3.2.9 Liquidity of Investments

a) Most short-term investments are held for cashflow management purposes and officers will ensure that sufficient levels of short-term investments and cash are available for the discharge of the Council's liabilities. Investment periods range from overnight to 364 days as specified investments or longer as a non-specified investment.

b) The average period of each investment in the current financial year, measured up to 31 December 2007, is 55.6 days. When deciding the length of each investment, regard is had to both cashflow needs and prevailing interest rates.

c) As referred to in paragraph 3.2.8(d) above it is recommended that a maximum of £5m be invested for periods exceeding 364 days (if interest rates are favourable) and the balance be held in short term investments (under 365 days).

3.2.10 Interest Rates

a) London Interbank Bid (LIBID) rates have risen during 2007-08 as illustrated below. Seven-day rates are more volatile as they are more susceptible to changes driven by market forces.

Movement in LIBID Rates

Date	7 Day	1 Month	3 Month
1 April 2007	5.32%	5.41%	5.55%
30 June 2007	5.80%	5.82%	5.94%
30 September 2007	5.78%	5.92%	6.13%
31 December 2007	5.79%	5.91%	5.89%

b) As referred to in paragraph 3.2.4(b) above, bank base rate currently stands at 5.25% and is forecast to reduce to 4.75% during 2008-09. Short-term interest rates are likely to average around these levels.

c) The Council maintains predominately temporary, short-term investments, which are made with reference to cash flow requirements.

d) For short term and overnight investment the Council makes full use of appropriate bank and building society call and deposit accounts which offer very competitive rates and in most instances instant access to funds.

3.2.11 Prudential indicators

The prudential indicators that relate to the Investments Strategy are reproduced at **Annex B**. These are:

a) Upper limits on variable interest rate exposure;

b) Upper limits on fixed interest rate exposures; and

c) Investments exceeding 364 days.

Other Issues

3.2.12 Sensitivity of Forecast

The majority of the Council's long-term debt is in the form of Money Market LOBO (Lenders Option, Borrowers Option) loans. Officers consider that the degree of risk on these loans attached to small variations in interest rates is low.

The main sensitivities of the forecast are likely to be the two scenarios below and only apply to new borrowing and investments. Officers, in conjunction with the Council's treasury advisors, will continually monitor both the prevailing interest rates and market forecasts, adopting the following responses to a change of view:

a) If it was felt that there was a significant risk of a sharp rise in long and short term rates, perhaps arising from a greater than expected increase in world economic activity or further increases in inflation. In this event the portfolio position will be re-appraised with the likely action that fixed rate loans will be taken whilst interest rates are still relatively cheap.

b) If it was felt that there was a significant risk of a sharp fall in long and short term rates due to growth rates weakening. In this event long term borrowings will be postponed, and potential rescheduling from fixed rate funding into variable or short rate funding will be considered.

3.2.13 Debt Financing Budget 2008-09 to 2010-11

The Debt Financing Budget has been prepared in accordance with the assumptions outlined above, and is attached at **Annex D** for information. The Cabinet is asked to note the proposed Debt Financing Budget, which is included in the Council Wide Revenue Budget, elsewhere on this agenda.

3.2.14 Council Policy on Reserves and Balances

The Council Wide Revenue Budget 2008-09 to 2010-11 report, elsewhere on this agenda, includes the Council's policy on reserves and balances – i.e. to protect balances wherever possible to allow the option of supporting future years' budgets, aiming for a minimum level of unallocated general fund reserves of £2.75m at the end of 2008/09 having regard to the outcome of the financial risk assessment

The Debt Financing Strategy has been prepared on the basis of that underlying policy.

3.2.15 Balanced Budget Requirement

The CIPFA Code of Practice on Treasury Management requires this report to include a reference to compliance under the Local Government Act 2003 to produce a balanced budget. Such compliance is demonstrated within the Council Wide Revenue Budget 2008-09 to 2010-11 report contained elsewhere on this agenda.

3.2.16 Treasury Management Practices (TMPs)

The Council's Treasury Management Practices (TMPs) set out the manner in which the Council will seek to achieve its treasury management policies and objectives and how it will manage and control those activities. The TMPs were agreed by Cabinet on 3 July 2006. They should be reviewed on a regular basis, and this will be undertaken during 2008-09 and reported to Cabinet.

3.3 Choices (Options)

3.3.1 Cabinet are asked to agree the recommendations at paragraph 2 above.

4. Implications (including financial implications)

4.1 Policy

4.1.1 The Treasury Strategy report sets the Council's policy on its debt and investment portfolios over the next and following two financial years. It is revisited annually and reported to Cabinet and Council as part of the budget setting process

4.2 Resources and Risk

4.2.1 The report pertains to the management of the Council's debt and investment portfolios, and resources and risk are dealt with in the main body of the report.

4.2.2 The risk management of the treasury function is considered as an integral part of day-to-day treasury activities, and is also specifically covered in the Council's Treasury Management Practices (TMPs).

4.3 Legal

4.3.1 The Council is obliged to carry out its treasury management activities in line with statutory requirements and associated regulations and professional guidance. The relevant legislative and regulatory documents are referred to within the report and listed in the background papers.

4.4 Equality

4.4.1 There are no specific equalities issues or implications associated with this report.

4.5 Consultees (Internal and External)

4.5.1 Consultation on treasury management matters is undertaken as appropriate with the Council's treasury advisers, Sector, and with the Portfolio holder for Finance.

4.6 How the Proposals deliver Priority Outcomes

4.6.1 The Audit Commission Key Lines of Enquiry for the Use of Resources (Financial Standing) requires the Council to "keep its treasury management strategy under review and monitor against it. The strategy [should] reflect the requirements of the CIPFA Code of Practice for Treasury Management in the Public Services"

4.7 Other Implications

4.7.1 No other implications have been identified.

5. Background Papers

Statute, Regulation and Guidance

CIPFA Treasury Management in the Public Services - Code of Practice and Cross-Sectoral Guidance Notes 2001

Local Government Act 2003

Local Authorities (Capital Finance and Accounting) (England) Regulations 2003

ODPM Guidance on Local Government Investments 2004

CIPFA Treasury Management in the Public Services - Guidance Notes for Local Authorities including Police Authorities and Fire Authorities (Fully Revised Second Edition 2006)

The Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008

CIPFA Prudential Code for Capital Finance in Local Authorities 2003

CIPFA Prudential Code for Capital Finance in Local Authorities – Fully Revised Guidance Notes for Practitioners 2007

Reports to Cabinet & Council

Capital Programme 2006-07 Monitoring – Report to Cabinet 3 July 2006 (Contains the Council's Treasury Management Practices (TMPs)

Capital Programme 2008-09 to 2012-13 - Report to Cabinet 20 February 2008

Council Wide Revenue Budget 2008-09 to 2010-11 - Report to Cabinet 20 February 2008

Housing Revenue Account (HRA) Budget 2008/09 and Rent Setting - Report to Cabinet 20 February 2008

Prudential Indicators for Capital Finance 2008-09 to 2010-11 - Report to Cabinet 20 February 2008

Prudential indicators for Capital Finance 2007-08 - Position as at 30 November 2007 - Report to Council 21 January 2008 (Contains formal adoption of the CIPFA Code of Practice for Treasury Management)

Bev Dixon, Finance Manager – Capital & Treasury, ext 7401

CABINET REPORT

SIGNATORIES

Report Title	**TREASURY STRATEGY 2008-09 TO 2010-11**
Date Of Call-Over	

Following Call-Over and subsequent approval by Management Board, signatures are required for all Key Decisions before submitting final versions to Meetings Services.

Name	Signature	Date	Ext.
Monitoring Officer or Deputy			
Section 151 Officer or Deputy			