TREASURY STRATEGY

1 Introduction

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.

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.

1.3 The Prudential Code requires the Council to set a number of prudential indicators for capital finance. The prudential indicators for 2008-09 to 2010-11 were agreed at Council on 28 February 2008. This strategy includes those prudential indicators to which regard should be given when considering the Council's Treasury Management Strategy for the next three financial years.

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

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

2 Capital Financing and Borrowing Strategy

2.1 The Capital Financing and Borrowing Strategy covers:

- Capital financing (2.2)
- New borrowing (2.3)
- Interest rate exposure (2.4)
- Prudential indicators (2.5)
- Temporary borrowing (2.6)

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 the Council may use borrowing where the Government awards borrowing approvals in the form of Supported Capital Expenditure (Revenue) (SCE(R)) and provide associated revenue support through the formula grant. Alternatively borrowing is available when other financing sources are not, in which circumstances unsupported (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 £25.9m. 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 came into force on 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. The detailed policy will be brought to Council for consideration in 2008-09.

   For the next 3 years MRP, calculated under previous 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 2.3 below.

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 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) 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.

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 20 October 2008.

Long Term Borrowing Rates - PWLB Maturity Loan Interest Rates			
	10 Years	**25 Years**	**50 Years**
2008-09			
Actual 1 April 2008	4.51%	4.53%	4.43%
Actual 1 July 2008	5.34%	4.86%	4.58%
Actual 1 October 2008	4.66%	4.75%	4.64%
Forecast Quarter 4	4.40%	4.55%	4.50%
2009-10			
Forecast Quarter 1	4.00%	4.45%	4.50%
Forecast Quarter 2	3.90%	4.50%	4.50%
Forecast Quarter 3	3.85%	4.50%	4.50%
Forecast Quarter 4	4.00%	4.50%	4.50%
2010-11			
Forecast Quarter 1	4.25%	4.55%	4.50%
Forecast Quarter 2	4.35%	4.60%	4.60%
Forecast Quarter 3	4.55%	4.70%	4.65%

LOBO rates on offer for 70-year loans at 20 October 2008 were at 4.35% and below, dependant on the initial fixed period of the loan.

The Council's Borrowing Strategy for 2008-09 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 2008/09 at 5.25% but this was reduced to 5% on 10 April 2008. This was reduced again to 4.5% as part of a package of measures to address the global economic crisis on 8 October 2008.

The current Sector forecasts indicate that the base rate will decline over the next 12 months before rising again in 2010-11. However, there is some difference of opinion among economists.

	Base Rate
2008-09	
Actual at 1 April 08	5.25%
Actual at 10 April 08	5.00%
Actual at 8 October 08	4.50%
Forecast Quarter 4	4.00%
2009-10	
Forecast Quarter 1	3.50%
Forecast Quarter 2	3.25%
Forecast Quarter 3	3.00%
Forecast Quarter 4	3.00%
2010-11	
Forecast Quarter 1	3.25%
Forecast Quarter 2	3.50%
Forecast Quarter 3	3.75%

* Date of Rate Change

2.5 Prudential indicators

The prudential indicators that relate to the Capital Financing and Borrowing Strategy are:

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

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

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

Operational boundary for external debt				
	2007-08 Boundary £000	2008-09 Boundary £000	2009-10 Boundary £000	2010-11 Boundary £000
Borrowing	40,500	36,000	36,000	36,000
Other long-term liabilities	0	2,000	2,000	2,000
TOTAL	40,500	38,000	38,000	38,000

c) Maturity structure of borrowing.

Maturity structure of borrowing		
	Lower Limit %	Upper Limit %
Under 12 months	0%	25%
1-2 years	0%	25%
2-5 years	0%	50%
5-10 years	0%	100%
Over 10 years	0%	100%

Maturity Periods of Council Borrowing	2008-09 Actual at 31 August 08
	%
Under 12 months	0.68
12 months and within 24 months	0.05
2 years and within 5 years	0.20
5 years and within 10 years	60.39
10 years and above	38.68

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 – Northampton Volunteer Bureau, and Billing Parish Council. 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 are working on setting up formal agreements with these organisations, incorporating a defined method of calculating the interest rate to be applied.

3 Investments Strategy

3.1 The Investments Strategy covers:

- Investments (3.1)
- Liquidity of Investments (3.2)
- Interest Rates (3.3)
- Prudential indicators (3.4)

3.2 Investments

a) Under the Local Government Act 2003 the Council is required to have regard to the CLG (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 CLG 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.

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.

This list may be further restricted with the approval of the Chief Finance Officer to limit the exposure of the authority to risk in times of economic or market uncertainty. Any adjustments in maximum lending limits under this paragraph will be reported to Cabinet subsequently.

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 cash flow management.

The maximum amount that the Council will hold at any time during the year as long-term investments is £6m. This is approximately 10% of the forecast average level of total investments in 2008-09, which is around £58m. This level of investment could be undertaken without having an adverse effect on cash flow.

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

3.3 Liquidity of Investments

a) Most short-term investments are held for cash flow 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 cash flow needs and prevailing interest rates.

3.4 Interest Rates

a) London Interbank Bid (LIBID) 3-month rates have risen during 2008-09 as illustrated below. Seven-day and one-month 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
31 December 2007	5.79%	5.91%	5.89%
1 April 2008	5.32%	5.65%	5.88%
30 June 2008	5.08%	5.38%	5.82%
30 September 2008	5.22%	5.95%	6.18%

b) As referred to above, bank base rate currently stands at 4.5% and is forecast to continue decline during 2008-09 and 2009-10. Short-term interest rates are likely to average slightly above 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.