

## Treasury Management Strategy and Investment Strategy 2015/16 to 2017/18

### 1. Summary

- 1.1. The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") and the Prudential Code require authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators (PIs) on an annual basis. The TMSS also includes the Annual Investment Strategy (AIS) that is a requirement of the Department for Communities and Local Government's (DCLG) Investment Guidance.
- 1.2. As per the requirements of the Prudential Code, Hampshire Fire and Rescue Authority adopted the CIPFA Treasury Management Code at its meeting in February 2012. This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the CLG Guidance.
- 1.3. The purpose of this TMSS is, therefore, to approve:
  - Treasury Management Strategy for 2015/16
  - Annual Investment Strategy for 2015/16
  - Prudential Indicators for 2015/16, 2016/17 and 2017/18 shown in Annex C
  - Minimum Revenue Provision (MRP) Statement shown in Annex D
- 1.4. The Fire and Rescue Authority has potentially large exposures to financial risks including the loss of invested funds and the effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Authority's treasury management strategy.
- 1.5. **This Report recommends the following be approved:**
  - **Treasury Management Strategy and Annual Investment Strategy for 2015/16, (and for the rest of 2014/15) including:**
    - **Prudential Indicators for 2015/16, 2016/17 and 2017/18 – Annex C**
    - **Minimum Revenue Provision (MRP) Statement – Annex D**
  - **That authority is delegated to the Treasurer to manage the Authority's investments according to the risk assessment process in the Investment Strategy as appropriate to most effectively manage the Authority's investments.**

## **2. Introduction**

- 2.1. In February 2012 the Fire and Rescue Authority adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year.
- 2.2. In addition, the Department for Communities and Local Government (CLG) issued revised Guidance on Local Authority Investments in March 2010 that requires the Authority to approve an investment strategy before the start of each financial year.
- 2.3. This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the CLG Guidance.
- 2.4. The Authority has potentially large exposures to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Authority's treasury management strategy.

## **3. External Context**

- 3.1. The following paragraphs explain the economic and financial background against which the Treasury Management Strategy is being set.

### **Economic background**

- 3.2. There is momentum in the UK economy, with a continued period of growth through domestically-driven activity and strong household consumption. There are signs that growth is becoming more balanced. The greater contribution from business investment should support continued, albeit slower, expansion of GDP. However, inflationary pressure is benign and is likely to remain low in the short-term. There have been large falls in unemployment but levels of part-time working, self-employment and underemployment are significant and nominal earnings growth remains weak and below inflation.
- 3.3. The Bank of England's Monetary Policy Committee's (MPC) focus is on both the degree of spare capacity in the economy and the rate at which this will be used up, factors prompting some debate on the Committee. Despite two MPC members having voted for an 0.25% increase in rates at each of the meetings August 2014 onwards, some Committee members have become more concerned that the economic outlook is less optimistic than at the time of the August Inflation Report.

### **Interest rate forecast**

- 3.4. The Authority's treasury management advisor Arlingclose forecasts the first rise in official interest rates in August 2015 and a gradual pace of increases thereafter, with the average for 2015/16 being around 0.75%. Arlingclose believes the normalised level of the Bank Rate post-crisis to range between 2.5% and 3.5%. The risk to the upside (i.e. interest rates being higher) is weighted more towards the end of the forecast horizon. On the downside, Eurozone weakness and the threat of deflation have increased the risks to the

durability of UK growth. If the negative indicators from the Eurozone become more entrenched, the Bank of England will likely defer rate rises to later in the year. A more detailed economic and interest rate forecast provided by the Arlingclose is attached at Annex A.

### Credit outlook

- 3.5. The transposition of two European Union directives into UK legislation in the coming months will place the burden of rescuing failing EU banks disproportionately onto unsecured local authority investors. The Bank Recovery and Resolution Directive promotes the interests of individual and small businesses covered by the Financial Services Compensation Scheme and similar European schemes, while the recast Deposit Guarantee Schemes Directive includes large companies into these schemes. The combined effect of these two changes is to leave public authorities and financial organisations (including pension funds) as the only senior creditors likely to incur losses, having to 'bail-in' a failing bank after July 2015.
- 3.6. The continued global economic recovery has led to a general improvement in credit conditions since last year. This is evidenced by a fall in the credit default swap spreads of banks and companies around the world. However, due to the above legislative changes, the credit risk associated with making unsecured bank deposits will increase relative to the risk of other investment options available to the Authority. Whilst the likelihood of suffering a loss from the default of a bank remains relatively unchanged, the 'bail-in' regime has significantly increased the impact a default would have in terms of the scale of loss the Authority could be exposed to.

## 4. Local Context

- 4.1. The Authority currently has £8.4m of borrowing and £31.1m of investments as at 31 December 2014. This is set out in further detail at Annex B. Forecast changes in these sums are shown in the balance sheet analysis in Table 1.

**Table 1: Balance Sheet Summary and Forecast**

	31.3.14 Actual £m	31.3.15 Revised £m	31.3.16 Estimate £m	31.3.17 Estimate £m	31.3.18 Estimate £m
Capital Financing Requirement	14.0	13.3	12.7	12.2	11.7
Less: External borrowing					
- Public Works Loan Board	(8.4)	(8.4)	(8.4)	(8.4)	(8.4)
- Finance Leases	(0.3)	(0.1)	0.0	0.0	0.0
<b>Internal (over) borrowing</b>	<b>5.3</b>	<b>4.8</b>	<b>4.3</b>	<b>3.8</b>	<b>3.3</b>
Less: Working capital	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Less: Usable reserves	(29.2)	(28.5)	(20.6)	(14.4)	(11.4)
<b>New borrowing or (investments)</b>	<b>(24.0)</b>	<b>(23.8)</b>	<b>(16.4)</b>	<b>(10.7)</b>	<b>(8.2)</b>

- 4.2. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Authority's current strategy is to maintain borrowing and investments below their underlying levels, known as internal borrowing.
- 4.3. The Authority's CFR will fall gradually over the coming years with the ongoing payment of Minimum Revenue Provision (MRP). The Authority's reserves are also planned to reduce as they are used to fund the capital programme. This will result in a reduction in overall investment balances, but not to the extent that the authority cannot continue its policy of internal borrowing, if this continues to be advantageous.
- 4.4. CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation during 2015/16.

## **5. Borrowing Strategy**

- 5.1. The Authority currently holds £8.4 million of loans as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in Table 1 shows that the Authority does not expect to need to borrow in 2015/16. The Authority may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £18.2 million.

### **Objectives**

- 5.2. The Authority's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the Authority's long-term plans change is a secondary objective.

### **Strategy**

- 5.3. Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to use internal resources.
- 5.4. By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise.
- 5.5. In addition, the Authority may borrow short-term loans (normally for up to one month) to cover unexpected cash flow shortages.

## **Sources**

- 5.6. The approved sources of long-term and short-term borrowing are:
- Public Works Loan Board (PWLB)
  - UK local authorities
  - any institution approved for investments (see below)
  - any other bank or building society authorised to operate in the UK
  - UK public and private sector pension funds (except the Hampshire Pension Fund)
  - capital market bond investors
  - special purpose companies created to enable local authority bond issues
- 5.7. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
- operating and finance leases
  - hire purchase
  - Private Finance Initiative
  - sale and leaseback
- 5.8. The Authority has previously raised the majority of its long-term borrowing from the PWLB but it continues to investigate other sources of finance, such as local authority loans and bank loans that may be available at more favourable rates.

### **Short-term and Variable Rate loans**

- 5.9. These loans leave the Authority exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators below.

### **Debt Rescheduling**

- 5.10. The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Authority may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

## **6. Investment Strategy**

- 6.1. The Authority holds invested funds representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's investment balance has ranged between £24.3 and £41.5 million, and similar levels are expected to be maintained in the forthcoming year.

## Objectives

- 6.2. Both the CIPFA Code and the CLG Guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk receiving unsuitably low investment income.

## Strategy

- 6.3. Due to the increasing risk from bank 'bail-ins' and continued low returns from short-term unsecured bank investments, the Authority aims to further diversify into more secure and/or higher yielding asset classes during 2015/16. This is especially the case for the estimated £17m that is available for longer-term investment. The majority of the Authority's surplus cash is currently invested in short-term unsecured bank deposits, certificates of deposit and money market funds. This diversification will therefore represent a substantial change in strategy over the coming year.

## Investment Limits

- 6.4. Given the impact of the Bank Recovery and Resolution Directive, and the recast Deposit Guarantee Schemes Directive, which has increased the credit risk that unsecured bank/building society investments could be 'bailed-in', the following investment limits are proposed to mitigate the risk whilst allowing sufficient flexibility to manage the Authority's investment balances.
- 6.5. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Maximum limits will also be placed on fund managers, foreign countries and industry sectors as below:

**Table 2: Investment Limits**

	<b>Cash limit</b>
Any single organisation, except the UK Central Government	£7m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£7m per group
Any group of pooled funds under the same management	£7m per manager
Registered Providers	£8m in total
Money Market Funds	50% in total

## Approved Counterparties

- 6.6. The Authority may invest its surplus funds with any of the counterparty types in Table 3, subject to the cash limits (per counterparty) and the time limits shown.

**Table 3: Approved Investment Counterparties and Limits**

<b>Credit Rating</b>	<b>Banks Unsecured</b>	<b>Banks Secured</b>	<b>Government</b>	<b>Corporates</b>	<b>Registered Providers</b>
UK Govt	n/a	n/a	£ Unlimited 30 years	n/a	n/a
AAA	£4m 5 years	£7m 20 years	£7m 30 years	£4m 20 years	£4m 20 years
AA+	£4m 5 years	£7m 10 years	£7m 25 years	£4m 10 years	£4m 10 years
AA	£4m 4 years	£7m 5 years	£7m 15 years	£4m 5 years	£4m 10 years
AA-	£4m 3 years	£7m 4 years	£7m 10 years	£4m 4 years	£4m 10 years
A+	£4m 2 years	£7m 3 years	£4m 5 years	£4m 3 years	£4m 5 years
A	£4m 13 months	£7m 2 years	£4m 5 years	£4m 2 years	£4m 5 years
A-	£4m 6 months	£7m 13 months	£4m 5 years	£4m 13 months	£4m 5 years
BBB+	£2m 100 days	£4m 6 months	£2m 2 years	£2m 6 months	£2m 2 years
BBB or BBB-	£2m next day only	£4m 100 days	n/a	n/a	n/a
None	£1m 6 months	n/a	£4m 25 years	n/a	£4m 5 years
Pooled funds	£7m per fund				

This table must be read in conjunction with the notes below

### **Credit Rating**

- 6.7. Investment decisions are made by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used.

### **Banks Unsecured**

- 6.8. Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. Unsecured investment with banks rated BBB or BBB- are restricted to overnight deposits at the Authority's current account at NatWest (which is currently rated as BBB+).

### **Banks Secured**

- 6.9. Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank/building society's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank/building society will not exceed the cash limit for secured investments.

### **Government**

- 6.10. Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 30 years.

### **Corporates**

- 6.11. Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Investing with any unrated corporate entity will be judged on a case-by-case basis and only considered if suitable security can be obtained for the Authority's investment.

### **Registered Providers**

- 6.12. Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services, they retain a high likelihood of receiving government support if needed.

### **Pooled Funds**

- 6.13. Shares in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Money Market Funds that offer same-day liquidity and aim for a constant net asset value will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.
- 6.14. Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

## **Risk Assessment and Credit Ratings**

- 6.15. Credit ratings are obtained and monitored by the Authority's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:
- no new investments will be made,
  - any existing investments that can be recalled or sold at no cost will be, and
  - full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.
- 6.16. Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

## **Other Information on the Security of Investments**

- 6.17. The Authority understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.
- 6.18. Based on the available information and the advice of the Authority's advisers, Arlingclose, the Treasurer may reduce the investment limits shown in Tables 2 and 3, and suspend investing with certain counterparties as necessary.
- 6.19. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

## **Specified Investments**

- 6.20. The CLG Guidance defines specified investments as those:
- denominated in pound sterling,
  - due to be repaid within 12 months of arrangement,
  - not defined as capital expenditure by legislation, and invested with one of:
    - the UK Government,
    - a UK local authority, parish council or community council, or

- a body or investment scheme of “high credit quality”.
- 6.21. The Authority defines “high credit quality” organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of A- or higher.

#### **Non-specified Investments**

- 6.22. Any investment not meeting the definition of a specified investment is classed as non-specified. The Authority does not intend to make any investments denominated in foreign currencies. Non-specified investments will therefore be limited to long-term investments, (i.e. those that are due to mature 12 months or longer from the date of arrangement), pooled funds that the Authority intends to hold as long-term investments (for more than a year) and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in Table 4 below.

**Table 4: Non-Specified Investment Limits**

	<b>Cash limit</b>
Total long-term investments	£17m
Total investments without credit ratings or rated below A- (excluding investments with other local authorities)	£15m
Total non-Sterling investments	£0m
Total investments in foreign countries rated below AA+	£0m
<b>Total non-specified investments</b>	<b>£32m</b>

#### **Liquidity Management**

- 6.23. The Authority has due regard for its future cash flows when determining the maximum period for which funds may prudently be committed. Historic cash flows are analysed in addition to significant future cash movements, such as payroll, grant income and council tax precept. Limits on long-term investments are set by reference to the Authority’s medium term financial position (summarised in Table 1) and forecast short-term balances.

### **7. Treasury Management Indicators**

- 7.1. The Authority measures and manages its exposures to treasury management risks using the following indicators.

#### **Interest Rate Exposures**

- 7.2. This indicator is set to control the Authority’s exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the amount of principal borrowed or invested will be:

	2015/16	2016/17	2017/18
Upper limit on fixed interest rate investment exposure	£17.0m	£15.0m	£15.0m
Upper limit on variable interest rate investment exposure	£50.0m	£50.0m	£50.0m
Upper limit on fixed interest rate borrowing exposure	£15.5m	£15.0m	£14.5m
Upper limit on variable interest rate borrowing exposure	£15.5m	£15.0m	£14.5m

- 7.3. Fixed rate investments and borrowings are those where the rate of interest is fixed for the whole financial year. Short-term instruments (with a maturity of less than one year) are classed as variable rate.

#### **Maturity Structure of Borrowing**

- 7.4. This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

	Upper	Lower
Under 12 months	50%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and within 20 years	75%	0%
20 years and above	100%	0%

- 7.5. Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

#### **Principal Sums Invested for Periods Longer than 364 days**

- 7.6. The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to final maturities beyond the period end will be:

	2015/16	2016/17	2017/18
Limit on principal invested beyond 364 days	£17m	£15m	£15m

## **8. Other Items**

- 8.1. There are a number of additional items that the Authority is obliged by CIPFA or CLG to include in its Treasury Management Strategy.

### **Policy on Use of Financial Derivatives**

- 8.2. In the absence of any legal power to do so, the Authority will not use standalone financial derivatives (such as swaps, forwards, futures and options). Derivatives embedded into loans and investments, including pooled funds, may be used, and the risks that they present will be managed in line with the overall treasury risk management strategy.

### **Investment Training**

- 8.3. The needs of the Authority's treasury management staff for training in investment management are assessed annually as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.
- 8.4. Staff regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, the Association of Corporate Treasurers and other appropriate organisations.
- 8.5. CIPFA's Code of Practice requires that the Authority ensures that all 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. Members of the Finance and General Purposes Committee were invited to a workshop presented by Arlingclose on 28 November 2014, which gave an update on treasury matters.

### **Investment Advisers**

- 8.6. The Authority has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues. The quality of this service is controlled through quarterly review meetings with the Treasurer and his staff and Arlingclose.

### **Investment of Money Borrowed in Advance of Need**

- 8.7. The Authority may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the Authority is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Authority's overall management of its treasury risks. The total amount borrowed will not exceed the authorised borrowing limit of £18.2 million.

## Annex A – Arlingclose Economic & Interest Rate Forecast October 2014

### Forecast:

- Arlingclose continues to forecast the first rise in official interest rates in Q3 2015; general market sentiment is now close to this forecast. There is momentum in the economy, but inflationary pressure is benign and external risks have increased, reducing the likelihood of immediate monetary tightening.
- We project a slow rise in Bank Rate. The pace of interest rate rises will be gradual and the extent of rises limited; we believe the normalised level of Bank Rate post-crisis to range between 2.5% and 3.5%.
- The short run path for gilt yields is flatter due to the deteriorating Eurozone situation. We project gilt yields on an upward path in the medium term.

	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Dec-17	Mar-18
<b>Official Bank Rate</b>													
Upside risk		0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.75	1.75
Downside risk				0.25	0.25	0.50	0.50	0.75	0.75	1.00	1.00	1.00	1.00
<b>3-month LIBID rate</b>													
Upside risk	0.05	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.55	0.60	0.65	0.85	1.00	1.15	1.30	1.45	1.60	1.75	1.85	2.05	2.15
Downside risk	0.10	0.15	0.20	0.30	0.40	0.55	0.65	0.75	0.85	-0.95	-0.95	-0.95	-1.00
<b>1-yr LIBID rate</b>													
Upside risk	0.10	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.95	1.00	1.05	1.20	1.35	1.50	1.65	1.80	1.95	2.10	2.20	2.40	2.50
Downside risk	-0.30	-0.35	-0.40	-0.45	-0.50	-0.55	-0.60	-0.65	-0.70	-0.75	-0.80	-0.80	-0.80
<b>5-yr gilt yield</b>													
Upside risk	0.30	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55
Arlingclose Central Case	1.70	1.75	1.90	2.00	2.10	2.20	2.30	2.40	2.50	2.60	2.70	2.90	2.95
Downside risk	-0.30	-0.35	-0.35	-0.35	-0.40	-0.45	-0.50	-0.55	-0.60	-0.65	-0.70	-0.70	-0.70
<b>10-yr gilt yield</b>													
Upside risk	0.30	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55
Arlingclose Central Case	2.40	2.45	2.55	2.60	2.65	2.70	2.75	2.80	2.85	2.90	2.95	3.05	3.10
Downside risk	-0.30	-0.35	-0.35	-0.35	-0.40	-0.45	-0.50	-0.55	-0.55	-0.55	-0.60	-0.60	-0.60
<b>20-yr gilt yield</b>													
Upside risk	0.30	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55
Arlingclose Central Case	2.90	2.95	3.05	3.10	3.15	3.20	3.25	3.30	3.35	3.40	3.45	3.50	3.55
Downside risk	-0.30	-0.35	-0.35	-0.35	-0.40	-0.45	-0.50	-0.50	-0.55	-0.55	-0.60	-0.60	-0.60
<b>50-yr gilt yield</b>													
Upside risk	0.30	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55
Arlingclose Central Case	3.00	3.05	3.10	3.15	3.20	3.25	3.30	3.35	3.40	3.45	3.50	3.55	3.60
Downside risk	-0.30	-0.35	-0.35	-0.35	-0.40	-0.45	-0.50	-0.55	-0.55	-0.55	-0.60	-0.60	-0.60

## Annex B – Existing Investment & Debt Portfolio Position

	31.12.2014 Actual Portfolio £m	31.12.2014 Average Rate %
<b>Borrowing:</b>		
Long-term loans - PWLB	8.4	4.7
Finance Leases	0.1	
<b>Total Gross External Debt</b>	<b>8.5</b>	
<b>Investments:</b>		
Direct Deposits		
- Barclays	2.0	
- Close Brothers	3.5	
- HSBC	3.5	
- Lloyds	1.0	
- Nationwide	3.0	
- Svenska Handelsbanken	0.3	
	<b>13.3</b>	<b>0.84</b>
Certificates of Deposit		
- Deutsche	3.5	
- Nordea	2.0	
- Rabobank	3.0	
- Standard Chartered	3.0	
	<b>11.5</b>	<b>0.73</b>
Property Funds		
- CCLA Property Fund	2.0	-
Other Local Authorities	3.0	0.91
Money Market Funds		
- Ignis	1.2	
- Federated	0.1	
	<b>1.3</b>	<b>0.47</b>
<b>Total Investments</b>	<b>31.1</b>	<b>0.79</b>
<b>Net Investments</b>	<b>22.6</b>	<b>-</b>

## Annex C - Prudential Indicators 2015/16

The Local Government Act 2003 requires the Authority to have regard to the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Authority has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

### Estimates of Capital Expenditure

The Authority's planned capital expenditure and financing is summarised as follows.

<b>Capital Expenditure and Financing</b>	<b>2014/15 Revised £m</b>	<b>2015/16 Estimate £m</b>	<b>2016/17 Estimate £m</b>	<b>2017/18 Estimate £m</b>
<b>Total Expenditure</b>	<b>5.3</b>	<b>17.9</b>	<b>7.0</b>	<b>3.9</b>
Capital Receipts	1.0	3.1	0.0	0.0
Government Grants	1.9	4.0	0.0	0.0
Reserves	0.0	6.2	6.0	2.9
Revenue	2.4	2.2	1.0	1.0
Capital contributions	0.0	2.4	0.0	0.0
Borrowing	0.0	0.0	0.0	0.0
<b>Total Financing</b>	<b>5.3</b>	<b>17.9</b>	<b>7.0</b>	<b>3.9</b>

### Estimates of Capital Financing Requirement

The Capital Financing Requirement (CFR) measures the Authority's underlying need to borrow for a capital purpose.

	<b>31.3.15 Revised £m</b>	<b>31.3.16 Estimate £m</b>	<b>31.3.17 Estimate £m</b>	<b>31.3.18 Estimate £m</b>
Capital Financing Requirement	13.3	12.7	12.2	11.7

The CFR is forecast to fall by £1.6m over the next three years as repayments are made via the MRP and there is no new capital expenditure being financed by debt.

### **Gross Debt and the Capital Financing Requirement**

In order to ensure that over the medium term debt will only be for a capital purpose, the Authority should ensure that debt 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. This is a key indicator of prudence.

<b>Debt</b>	<b>31.3.15 Revised £m</b>	<b>31.3.16 Estimate £m</b>	<b>31.3.17 Estimate £m</b>	<b>31.3.18 Estimate £m</b>
Borrowing	8.4	8.4	8.4	8.4
Finance leases	0.1	0.0	0.0	0.0
<b>Total Debt</b>	<b>8.5</b>	<b>8.4</b>	<b>8.4</b>	<b>8.4</b>

Total debt is expected to remain below the CFR during the forecast period.

### **Operational Boundary for External Debt**

The operational boundary is based on the Authority's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Authority's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance leases, and other liabilities that are not borrowing but form part of the Authority's debt.

<b>Operational Boundary</b>	<b>2014/15 Revised £m</b>	<b>2015/16 Estimate £m</b>	<b>2016/17 Estimate £m</b>	<b>2017/18 Estimate £m</b>
Borrowing	16.0	15.5	15.0	14.5
Other long-term liabilities	0.1	0.0	0.0	0.0
<b>Total Debt</b>	<b>16.1</b>	<b>15.5</b>	<b>15.0</b>	<b>14.5</b>

### **Authorised Limit for External Debt**

The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Authority

can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

<b>Authorised Limit</b>	<b>2014/15 Revised £m</b>	<b>2015/16 Estimate £m</b>	<b>2016/17 Estimate £m</b>	<b>2017/18 Estimate £m</b>
Borrowing	18.7	18.2	17.7	17.2
Other long-term liabilities	0.1	0.0	0.0	0.0
<b>Total Debt</b>	<b>18.8</b>	<b>18.2</b>	<b>17.7</b>	<b>17.2</b>

### Ratio of Financing Costs to 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 financing costs, net of investment income.

	<b>2014/15 Revised %</b>	<b>2015/16 Estimate %</b>	<b>2016/17 Estimate %</b>	<b>2017/18 Estimate %</b>
Ratio of Financing Costs to Net Revenue Stream	1.30%	1.22%	1.32%	1.39%

### Incremental Impact of Capital Investment Decisions

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax levels. The incremental impact is the difference between the total revenue budget requirement of the current approved capital programme and the revenue budget requirement arising from the capital programme proposed earlier in this report.

<b>Incremental Impact of Capital Investment Decisions</b>	<b>2015/16 Estimate £</b>	<b>2016/17 Estimate £</b>	<b>2017/18 Estimate £</b>
General Fund - increase in annual band D Council Tax	2.51	1.63	1.66

**Adoption of the CIPFA Treasury Management Code:** The Authority adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition in February 2012.

## **Annex D – Annual Minimum Revenue Provision Statement 2015/16**

Where the Authority finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Authority to have regard to the Department for Communities and Local Government's Guidance on Minimum Revenue Provision (the CLG Guidance) most recently issued in 2012.

The broad aim of the CLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The CLG Guidance requires the Authority to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP. The four MRP options available are:

- Option 1: Regulatory Method
- Option 2: CFR Method
- Option 3: Asset Life Method
- Option 4: Depreciation Method

### **MRP in 2015/16**

Options 1 and 2 may be used only for supported (i.e. financing costs deemed to be supported through Revenue Support Grant from Central Government) capital expenditure funded from borrowing. Methods of making prudent provision for unsupported capital expenditure include Options 3 and 4 (which may also be used for supported capital expenditure if the Authority chooses).

The Authority will apply Option 1/Option 2 in respect of supported capital expenditure funded from borrowing and Option 3/Option 4 in respect of unsupported capital expenditure funded from borrowing.

MRP in respect of leases and Private Finance Initiative schemes brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.

Capital expenditure incurred during 2015/16 will not be subject to a MRP charge until 2016/17.