| | |
|---|---|
| **Meeting:** | **Executive** |
| **Date:** | **11 January 2011** |
| **Subject:** | **Treasury Management Strategy** |
| **Report of:** | **Cllr Maurice Jones, Portfolio Holder for Corporate Resources** |
| **Summary:** | The report proposes a revised strategy in response to changes in two key codes and increased risk in investment markets. |

| | |
|---|---|
| Advising Officer: | Richard Ellis, Director of Customer and Shared Services |
| Contact Officer: | Matt Bowmer, Assistant Director Financial Services |
| Public/Exempt: | Public |
| Wards Affected: | All |
| Function of: | Council |
| Key Decision | Yes |
| Reason for urgency/ exemption from call-in (if appropriate) | N/A |

**CORPORATE IMPLICATIONS**

**Council Priorities:**

Not applicable.

**Financial:**

None directly arising from the report.

**Legal:**

Central Bedfordshire's Strategy is in line with the requirements of the Treasury Management in the Public Sector Code of Practice and The Prudential Code for Capital Finance in Local Authorities.

**Risk Management:**

The Strategy requires the consideration of risk in all treasury management undertakings.

**Staffing (including Trades Unions):**

None.

**Equalities/Human Rights:**

None.

**Community Safety:**

None.

**Sustainability:**

None.

**Summary of Overview and Scrutiny Comments:**

- The Customer and Central Services Overview and Scrutiny Committee considered the Strategy at its meeting on 13 December 2010. It recommended: 'That the Executive continues to minimise investments commensurate with risk in order to maximise the savings that would be realised by such action'.

**RECOMMENDATION(S):**

**That the Executive recommends Council to approve the Treasury Management Policy and the Treasury Management Strategy.**

| | |
|---|---|
| *Reason for Recommendation(s):* | *To put an effective treasury management framework in place for the Council.* |

**Executive Summary**

Central Bedfordshire annually agrees its Treasury Management Policy and Treasury Management Strategy. In response to the greater risk and uncertainty in investment markets CIPFA revised both the Treasury Management Code of Practice and the Prudential Code for Capital Finance in Local Authorities in the autumn of 2009. There continues to be a greater focus on risk in the two codes and this is recognised in the strategy.

Due to the continued lack of confidence in the markets the Strategy seeks to diversify the investment portfolio. There has been some recapitalisation of the UK banking institutions and this enables longer term lending, up to two years, to take place.

**Introduction**

1. Local authority investments have been placed under greater scrutiny following the failure of the Icelandic Banks. In March 2009 the Audit Commission published their 'Risk and Return' report, the recommendations from which were addressed in the revised Treasury Management in the Public Sector Code of Practice. The Prudential Code for Capital Finance in Local Authorities was also revised in light of the greater risk now evident in investment markets.

2. The Treasury Management Policy is attached for reference at Appendix A; this was revised last year and is subject to review every three years. There are no changes proposed.

3. A revised Treasury Management Strategy is attached at Appendix B. The authority considers its Treasury Management Strategy against the key objectives of being tactically flexible whilst maintaining control.

**Developments in Treasury Management in Central Bedfordshire Council**

4. The conclusion of the audit of the 2009/10 annual accounts has now provided the authority with its first balance sheet on which detailed projections can be made. This naturally allows the authority to better understand the relationship between its assets and liabilities and the levels of cash available to support them.

5. Analysis of the 2009/10 closing balance sheet reveals the following:

   a) The Council's Capital Financing Requirement is calculated by comparing the total valuation of the authority's fixed assets against the accumulated financing of these assets (e.g. through government grants deferred, borrowing applied through the Minimum Revenue Provision etc). This requirement represents the authority's underlying need to borrow and at £194M was above the actual level of external borrowing and, other long term liabilities of £178M. As a consequence, the authority is considered to be 'internally borrowed' by £16M;

   b) in common with many local authorities, the amount owed by the authority (creditors of £69M) significantly exceeded the amount owed to the authority (debtors of £56M). This working capital 'excess' reduces the level of borrowing required to support the longer term financing commitments.

6. The Capital Programme Review presented to November Executive included the planned intention of the authority to reduce its levels of borrowing in the short term in view of the affordability of the associated capital financing costs.

**Developments in Treasury Management**

7. The Decentralisation and Localism Bill 2010 will have a significant impact on treasury management. In essence, this will remove the existing subsidy system but transfer all debt back to the local authority. It is expected that the new system would start in April 2012. It will require the authority to fund the amount owed in the medium term through internal resources and/or external borrowing. The authority would have the option of borrowing from the PWLB or the wider financial market. This will require the authority to review its Prudential Indicators in the first quarter of the 2011/12 financial year. It is recommended that the Treasury Management Strategy is reviewed at this time and the Prudential Indicators reassessed accordingly.

8. The Spending Review announced the increase of new local authority fixed rate loans, undertaken through the Public Works and Loans Board (the statutory body operating within the Debt Management Office that is responsible for lending money to local authorities), This broadly equates to a 1% increase above existing rates. The implications of this development will be assessed on an ongoing basis with the authority's advisers, Arlingclose. In simple terms

future borrowing has become more expensive and this will need to be taken into account when council considers its Capital Programme in February 2011. Consequently there will be a greater imperative to balance the Programme through grants, contributions and capital receipts with less reliance on borrowing.

9. There are signs of stabilisation in market conditions resulting in wider opportunities and options for investments. This is evidenced through the resilience tests applied to banks that showed stability although these are subject to rigorous and ongoing review.

10. The path of interest base rates reflects the fragility of the economic recovery and the significantly greater fiscal tightening of the emergency budget. With growth and underlying inflation likely to remain subdued, the Bank of England is likely to remain with its 'lower for longer' stance on interest rates.

**Treasury Management Policy**

11. No changes are proposed for the Treasury Management Policy adopted by the Council in February 2010.

**Treasury Management Strategy 2011/12**

12. The current strategy and practices reflect the greater focus on risk demanded by the Treasury Management in the Public Services Code of Practice and Prudential Code for Capital Finance in Local Authorities**.**

13. It will be some time before confidence in the investment markets is fully restored and the number of institutions to whom the Council can lend remains restrictive (these are captured within a counterparty list). The Council constantly reviews its counterparty list with its advisors and as a consequence of the continued lack of confidence in markets has reduced the limits for individual counterparties. The Council will allow all existing investments to mature beyond 31 March 2010, where these are in excess of the revised limits. However, the Council will now look to make investments with counterparties for over 365 days and up to a maximum of two years. The current situation has eased sufficiently and this is evidenced by the banks making steps towards recapitalisation.

14. As a result of the review of the counterparty list, it is felt that there is sufficient confidence to add the following foreign institutions to the counterparty list. These are ING, Societe Generale and Svenska Handelsbanken. As with all institutions in the list they must be rated A+ by Fitch and Standard and Poor and A+ by Moody's before the authority can consider lending to them.

15. The authority has reviewed the potential sources of borrowing available with its advisers, Arlingclose. As a result of this review, it has chosen to extend its borrowing options to include Structured Finance and Medium Term Notes. Its preferred borrowing option remains PWLB and the new potential sources of borrowing are options only. Despite the 1% increase in rates on PWLB from 1 April 2011 it is likely to continue to be the most competitive option.

16. The Treasury Management Strategy sets out an Authorised Limit of £272M. This represents the maximum level of external borrowing on a gross basis and is the statutory limit determined under Section 3 (1) of the Local Government Act 2003. The Operational Boundary is set at £257M and links directly to the Capital Financing Requirement and estimates of other cashflow requirements. The Operational Boundary is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but excludes the additional headroom included within the Authorised Limit.

17. The Code of Financial Governance in the Council's Constitution makes provision for detailed Financial Procedures. The day to day operational guidance on treasury management practices are set on in Financial Procedure 16: Treasury Management.

**Monitoring Performance**

18. In line with the CIPFA Code, the Customer and Central Services Overview and Scrutiny Committee receive quarterly reports on the Authority's Treasury Management activities. This includes details of compliance with the Prudential Indicators as outlined within the Treasury Management Strategy. These are the Authorised Limit and the Operational Boundary. No breaches of the Prudential Indicators have been recorded within this financial year.

**Appendices:**

Appendix A Treasury Management Policy
Appendix B Treasury Management Strategy, February 2011

**Background Papers** (open to public inspection):

Treasury Management in the Public Sector Code of Practice, fully revised 2nd edition 2009
The Prudential code for Capital Finance in Local Authorities, fully revised 2nd edition 2009

Location of papers: Technology House, Bedford