ANNEX 2

Central Bedfordshire Council

Annual Treasury Management Strategy (including Investment Strategy 2009-10 to 2011-12)

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Appendices

Annual Treasury Management Strategy
(including Investment Strategy 2009-10 to 2011-12)

1. Background

1.1 The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") requires local authorities to set the Treasury Management Strategy (TMS) for borrowing each financial year.

1.2 CIPFA has defined Treasury Management as:

"the management of the organisation's cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.3 The Council will regard the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Treasury management risks are identified in the Council's approved Treasury Management Practices; the main risks to the Council's treasury activities are:

- Liquidity Risk (Inadequate cash resources)
- Market or Interest Rate Risk (Fluctuations in interest rate levels and thereby in the value of investments).
- Inflation Risks (Exposure to inflation)
- Credit and Counterparty Risk (Security of Investments)
- Refinancing Risks (Impact of debt maturing in future years).
- Legal & Regulatory Risk (i.e. non-compliance with statutory and regulatory requirements, risk of fraud).

1.4 The strategy also takes into account the outlook for interest rates, the Council's estimated opening treasury position and its Prudential Indicators recommended for approval (attached as Appendix A). The PIs relevant to the treasury management strategy are set out below:

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PI No.		2009-10 Estimate	2010-11 Estimate	2011-12 Estimate
6	Authorised Limit for External Debt	***£360m***	***£360m***	***£360m***
7	Operational Boundary for External Debt	***£350m***	***£350m***	***£350m***
9	Upper Limit for Fixed Interest Rate Exposure	***100%***	***100%***	***100%***
10	Upper Limit for Variable Rate Exposure	***50%***	***50%***	***50%***
12	Upper Limit for total principal sums invested over 364 days	***£20m***	***£20m***	***£20m***
11	Maturity structure of fixed rate borrowing :		Lower Limit %	Upper Limit %
	under 12 months		**0**	**100**
	12 months and within 24 months		**0**	**100**
	24 months and within 5 years		**0**	**100**
	5 years and within 10 years		**0**	**100**
	10 years and above		**0**	**100**

1.5 This TMSS also incorporates the Council's Investment Strategy.

2. The Treasury Position

2.1 The estimated opening treasury position at 01/04/2009 is as follows:

	£m
Debt	154
Investments	128
Net	26

3. Outlook for Interest Rates

The economic interest rate outlook and commentary is attached at Appendix B. This has been provided by Arlingclose Ltd, the treasury advisors currently engaged by Mid and South Beds Councils.

4. Borrowing Requirement and Strategy

4.1 The Council's underlying need to borrow for capital purposes is measured by reference to its Capital Financing Requirement (CFR). The CFR will determine the Council's requirement to make a Minimum Revenue Provision for Debt Redemption (MRP) from within its Revenue budget. Physical borrowing may be greater or less than the CFR. DCLG Guidance recommends that before the start of the financial year, a statement of MRP policy for the forthcoming financial year is approved by the Full Council. The proposed Annual MRP Statement is attached as Appendix C to this Strategy.

CFR	31/3/2010 Estimate £'000	31/3/2011 Estimate £'000	31/3/2012 Estimate £'000
Non-HRA	168,854	172,230	202,249
HRA	-7,739	-7,739	-7,739
Total CFR	**158,115**	**164,491**	**194,510**

4.2 In accordance with the Prudential Code, the Council will ensure that net external borrowing does not, except in the short term, exceed the CFR.

4.3 Capital expenditure not financed from internal resources (i.e. Capital Receipts, Capital Grants and Contributions, Revenue or Reserves) will produce an increase in the CFR (the underlying need to borrow) and may in turn produce an increased requirement to charge MRP in the Revenue Account.

4.4 The cumulative estimate of the long-term borrowing requirement is calculated as follows:

	31/3/2010 Estimate £'000	31/3/2011 Estimate £'000	31/3/2012 Estimate £'000
Capital Financing Requirement	158,115	164,491	194,510
Less: Existing Profile of Borrowing and Other Long Term Liabilities	154,146	154,146	154,146
Cumulative Borrowing Requirement	**3,969**	**10,345**	**40,364**

4.5 The Council will seek to maintain maximum control over its borrowing activities as well as flexibility on its loans portfolio. Capital expenditure levels, market conditions and interest rate levels will be monitored during the year in order to minimise borrowing costs over the medium to longer term. A prudent and pragmatic approach to borrowing will be maintained to minimise borrowing costs without compromising the longer-term stability of the portfolio, consistent with the Council's Prudential Indicators.

4.6 In conjunction with advice from any treasury advisory company that may be appointed, the Council will keep under review the options it has in borrowing from the PWLB, the market and other sources identified in the Treasury Management Practices Schedules up to the available capacity within its CFR and Affordable Borrowing Limit (defined by CIPFA as the Authorised Limit).

4.7 Short-dated gilt yields are forecast to be considerably lower than medium- and long-dated gilt yields during the financial year. Despite additional gilt issuance to fund the UK government's support to the banking industry, short-dated gilts are expected to benefit from expectations of lower interest rates as the economy struggles through a recession. Yields for these maturities will fall as expectations for lower interest rates mount.

4.8 The Council will consider and keep under review the relative merits of a strategic exposure to variable rate debt. Decisions to borrow at low, variable rates of interest will be taken after considering the absolute level of longer term interest rate equivalents and the extent of variable rate earnings on the Council's investment balances.

4.9 Actual borrowing undertaken and the timing will depend on capital expenditure levels, interest rate forecasts and market conditions during the year, in order to minimise borrowing costs. This may include borrowing in advance of future years' requirements provided that overall borrowing is maintained within the Council's projected CFR and its approved Authorised Borrowing Limit.

4.10 The Council will undertake a financial options appraisal process to establish how it has arrived at its 'value for money' judgement in the use of resources.

5. Debt Rescheduling

5.1 The Council will maintain a flexible policy for debt rescheduling. Market volatility may provide opportunities for rescheduling debt from time to time. The rationale for rescheduling would be one or more of the following:

- Savings in interest costs with minimal risk.
- Balancing the volatility profile (i.e. the ratio of fixed to variable rate debt) of the debt portfolio.
- Amending the profile of maturing debt to reduce any inherent refinancing risks.

5.2 The rescheduling of PWLB debt since the introduction of its repayment rates on 1st November 2007 has not ceased, but has become undoubtedly harder and places greater emphasis on the timing and type of new borrowing.

5.3 Any rescheduling activity will be undertaken within the Council's treasury management policy and strategy. The Council will determine in advance the strategy and framework within which debt will be repaid/rescheduled if opportunities arise. Thereafter the Council's debt portfolio will be monitored against equivalent interest rates and available refinancing options on a regular basis.

5.4 All rescheduling activity will comply with the accounting requirements of the local authority SORP and regulatory requirements of the Capital Finance and Accounting Regulations (SI 2007 No 573 as amended by SI 2008/414).

5.5 Any borrowing and debt rescheduling activity will be reported to a subsequent meeting of the Executive.

6. Investment Policy and Strategy

Background

6.1 Guidance from the DCLG on Local Government Investments in England requires, similarly, that an Annual Investment Strategy (AIS) be set. The Guidance permits the TMS and the AIS to be combined into one document.

Investment Policy

6.2 The Council's general policy objective will be to invest its surplus funds prudently. The Council's investment priorities are:

- security of the invested capital;
- liquidity of the invested capital;
- an optimum yield which is commensurate with security and liquidity.

The speculative procedure of borrowing purely in order to invest is unlawful.

6.3 The credit crisis has refocused attention on the treasury management priority of security of capital monies invested. The Council has reviewed its approach and assesses a wider range of indicators of credit strength than the pure reliance upon credit ratings. This includes a range of objective indicators (such as credit default swaps, share price movements and sovereign credit ratings and economic indicators) as well as a subjective overlay.

6.4 Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the DCLG Guidance.

6.5 Specified Investments will be those that meet the criteria in the DCLG Guidance, i.e. the investment

- is sterling denominated
- has a maximum maturity of 1 year
- meets the "high" credit criteria as determined by the Council or is made with the UK government or is made with a local authority in England, Wales and Scotland.
- the making of which is not defined as capital expenditure under section 25(1)(d) in SI 2003 No 3146 (i.e. the investment is not loan capital or share capital in a body corporate)

6.6 The Council's investments will be in the following investment instruments classified as Specified Investments:

- term deposits in banks and building societies;
- certificates of deposit with banks and building societies;
- other local authorities;
- money market funds with a AAAm rating and a constant net asset value;
- UK Government bonds (Gilts); and,
- UK Treasury Bills.

6.7 Non-Specified Investments will satisfy all the criteria of Specified Investments with one exception, they will have a maximum maturity of 6 years and the maximum exposure will be £20m. They will cover the following investments:

- Bonds issued by Multilateral Development Banks (i.e. European Investment Bank, World Bank);
- Bonds issued by institutions with an explicit UK Government Guarantee; and
- Certificates of deposit with banks and building societies,
- UK Government bonds (Gilts); and,
- Other local authorities.

6.8 The Director of Corporate Resources, under delegated powers, will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Decisions taken on the core investment portfolio will be reported to the Executive.

6.9 All investment activity will comply with the accounting requirements of the local authority SORP.

Investment Counterparties

6.10 Financial markets and financial institutions remain in a state of heightened risk as the impact of the credit crunch continues to adversely affect the global economy. The Council's investment activities have been restricted as a consequence in order to demonstrably address the prevailing higher risk backdrop.

6.11 The Council is able to invest in the investment instruments outlined in 6.6 and 6.7 above but investments in banks and building societies (on a term or certificate of deposit basis) should currently limited to UK banks and building societies that have a minimum AA- long term credit rating and F1+ short term rating <u>and</u> are participants in the UK Government's Credit Guarantee Scheme (CGS).

This currently limits activity to the following banks:

- Abbey National
- Barclays
- Clydesdale Bank
- HSBC
- Lloyds/HBOS
- Royal Bank of Scotland

and the following Building Society:

- Nationwide

The CGS effectively provides a UK Government Guarantee for these institutions, some of whom such as Lloyds/HBOS and Royal Bank of Scotland have been partially nationalised by the UK Government.

Deposits with these banks and building society are allowed for periods up to 12 months duration and £25m exposure limit per institution applies.

Given current conditions and the possibility of downgrade to the UK and its banks the Head of Financial services will have delegated power to allow the continuation of use of these six institutions even if they suffer downgrades below a long-term rating of AA- and a short-term rating of F1+.

6.12 The Council will need to have an account with the Debt Management Deposit Account Facility (DMADF). This facility allows the Council to invest with the UK Government via HM Treasury for periods up to 6 months. There should be no exposure limit on the DMADF as an investment counterparty.

6.13 The Council should also utilise Money Market Funds with a AAAm rating and operating on a constant net asset value basis (CNAV) and a 60 day Weighted Average Maturity (WAM). The Council can invest up to £10m in money market funds but has a maximum exposure limit to any one Fund of £5m.

6.14 Investments in other UK local authorities should be permitted, with no exposure limit as investment counterparties.

6.15 The Council should be permitted to invest in sterling denominated bonds issued by HM Government (Gilts), bonds issued with a HM Government Guarantee and bonds issued by Multi Lateral Development Banks (i.e. European Investment Bank, World Bank). Investments in these bonds will be for periods of up to 6 years.

6.16 The Council will inherit investment portfolios from Mid Beds Council managed externally, including the Lime Property Fund, which is a collective investment scheme, but classified as capital expenditure under Government Regulations.

6.17 The permitted **new** investments for Central Bedfordshire can be summarised as follows:

Investment	Maximum Counterparty Limit	Maximum Length of Investment	Criteria
Deposits and Certificates of Deposit with Banks and Building Societies	£25m	1 year	** Min AA long term category and F1+ short-term rating (or equivalent) plus CGS
Local Authorities	£10m per local authority, unlimited exposure to the sector	5 years	
Money Market Funds	£5m per Fund	n/a	AAAm and CNAV 60 Day WAM
Lime Property Fund	£5m	n/a	
Money Market Funds and Collective Investment Schemes (pooled funds which meet the definition of a collective investment scheme as defined in SI 2004 No 534 and SI 2007 No 573)	£10m per Fund	n/a	
DMADF	Unlimited		
HM Government (Gilts and Treasury Bills)	Unlimited	10 years	
Bonds issued by Multilateral Development Banks	£20m	10 years	
Bonds issued with HM Government Guarantee	£20m	10 years	

** In view of the high degree of uncertainty in financial markets, at the time of determining this strategy (February 2009), this list is currently limited to institutions which meet the credit criteria and can access the UK Government's Credit Guarantee Scheme (those listed in 6.11). As and when market conditions improve, the Director of Corporate Resources will include other institutions that satisfy the minimum credit criteria and will, as necessary, also align the maximum limit to reflect the increased number of counterparties.

Investment Strategy

6.18 With short term interest rates sharply lower and expected to decrease further in 2009, investment strategy would typically result in a lengthening of investment periods, where cash flow permits, in order to lock-in higher rates of acceptable risk adjusted returns. The problem in the current environment is finding an investment counterparty providing acceptable levels of counterparty risk.

Investment strategy will be to invest for longer periods (up to 5 years) in bonds issued by HM Government, Multilateral Development Banks and bonds with a HM Government Guarantee to secure a level of acceptable risk adjusted return that should span the period of sharply lower interest rates. The bonds satisfy the investment objectives of the Council and as Non Specified Investments any investment will be limited to a maximum of £20m.

Remaining investments will be placed with the other approved investment counterparties in order to achieve a diversified portfolio of prudent counterparties, investment periods and rates of return.

7. Balanced Budget Requirement

7.1 The Council complies with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

8. Reporting on the Treasury Outturn

8.1 The Head of Financial Services will report to the Executive on treasury management activity / performance as follows:
(a) Bi-monthly against the strategy approved for the year, including (b) below.
(b) The Council is required to produce an outturn report on its treasury activity no later than 30th September after the financial year end.

9. Other Issues

CIPFA review of the Prudential Code

9.1 In early 2008 CIPFA undertook a consultation exercise to review the implementation and ongoing use of the Prudential Code. CIPFA has yet to publish its conclusions arising from the consultation process. In the event that amendments are made to the Code by CIPFA, these may need to be reflected in the Treasury Management and Investment Strategy documentation.

Appointment of Treasury Advisors

9.2 In view of the complex nature of Treasury Management, the scale of the sums borrowed and invested and the high level of risk involved with such activity, the Council will consider appointing specialists who can provide independent, unbiased and bespoke advice on an ongoing basis.

Review of TMSS/IAS and Prudential Indicators

9.3 This strategy document and the prudential indicators have been prepared based on an estimation of the anticipated position of the new Council. Estimates have been prepared based on the combination of South Beds and Mid Beds, along with an assessment of the potential disaggregation of Bedfordshire County Council to Central Bedfordshire. It is therefore recommended that the Council undertakes a review of its position when the final accounts of the predecessor authorities have been closed and in particular when the actual disaggregation of Bedfordshire can be more accurately assessed. This is likely to be possible in the second half of 2009/10 at which time it may be appropriate to submit to members a further report on the Strategy and Prudential Indicators based on this review.

Implications of Local Government Review

9.4 In setting this policy there is one peculiarity arising from the creation of Central Bedfordshire. As the legal successor authority to Bedfordshire County Council, the Council will initially also be responsible for cash deposits placed by the County Council that mature after 31 March 2009. Disaggregation of these deposits will ultimately form part of the overall disaggregation settlement of the Bedfordshire County Council balance sheet between Central Bedfordshire and Bedford Borough Council.

The new Council will also inherit investment balances from both Mid Bedfordshire and South Bedfordshire District Councils. All three authorities had differing policies and therefore at inception Central Bedfordshire will be holding higher balances with some individual institutions than would normally be the case for Central Bedfordshire as an ongoing authority.

These will be managed out in due course, possibly early in 2009/10 when some initial arrangements with Bedford Borough Council are concluded. However, this unusual and temporary situation is outside the parameters of the proposed treasury management strategy.

PRUDENTIAL INDICATORS APPENDIX A

Prudential Indicators FY 2009-10 to FY 2011-12

1. Background

There is a requirement under the Local Government Act 2003 for local authorities to have regard to Cipfa's Prudential Code for Capital Finance in Local Authorities (the "Cipfa Prudential Code") when setting and reviewing their Prudential Indicators. It should be noted that CIPFA undertook a review of the Code in early 2008. The outcome from that review has yet to be published.

2. Estimates of Capital Expenditure

2.1 This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax and in the case of the HRA, housing rent levels.

No. 1	**Capital Expenditure**	**2009-10**	2010-11	2011-12
		Estimate £'000	Estimate £'000	Estimate £'000
	Non-HRA	**49,984**	60,000	52,578
	HRA	**5,686**	4,900	5,006
	Total	**55,670**	**64,900**	**57,584**

2.2 Capital expenditure will be financed as follows:

Non-HRA Capital Financing	**2009-10**	2010-11	2011-12
	Estimate £'000	Estimate £'000	Estimate £'000
Capital receipts	**8,787**	11,030	5,408
Government Grants	**24,471**	26,205	5,343
External Contributions	**7,849**	11,360	6,527
Earmarked Reserves	**20**	304	300
Revenue contributions	**70**	70	70
Supported borrowing	**8,787**	11,031	0
Unsupported borrowing	**0**	0	34,930
Total	**49,984**	60,000	52,578

HRA Capital Financing	**2009-10**	2010-11	2011-12
	Estimate £'000	Estimate £'000	Estimate £'000
Capital receipts	**1,694**	809	814
Major Repairs Allowance	**3,649**	3,748	3,849
Revenue contributions	**343**	343	343
Total	**5,686**	4,900	5,006

Note: the element to be financed from borrowing impacts on the movement in the CFR.

3. Ratio of Financing Costs to Net Revenue Stream

3.1 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 borrowing costs. The definition of financing costs is set out at paragraph 87 of the Prudential Code.

3.2 The ratio is based on costs net of investment income.

No. 2	**Ratio of Financing Costs to Net Revenue Stream**	**2009-10**	2010-11	2011-12
		Estimate %	Estimate %	Estimate %
	Non-HRA	**5.89**	6.15	6.69
	HRA	**0.64**	0.63	0.61
	Total	**5.28**	5.52	5.99

4. Capital Financing Requirement

4.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and its financing. It is an aggregation of the amounts shown for Fixed and Intangible assets, the Revaluation Reserve, the Capital Adjustment Account, Government Grants Deferred and any other balances treated as capital expenditure.

4.2 Options have been considered whereby the 2009/10 opening CFR position for Central Bedfordshire, and consequently the MRP, could be reduced by setting aside of the unapplied capital receipts of Mid Bedfordshire (estimated to be over £55 million as at 31 March 2009). This reduction would be achieved by setting aside receipts of around £23 million in the Capital Adjustment Account in the Mid Bedfordshire balance sheet as at 31 March 2009.This set aside is reflected in the calculation of the CFR shown below.

Approval of the precise amount of this set-aside will be considered by the Shadow Executive when it approves the final financing of the capital programmes of the predecessor authorities, prior to approval of the Statement of Accounts.

No. 3	**Capital Financing Requirement**	**31/03/10**	31/03/11	31/03/12
		Estimate	Estimate	Estimate
		£'000	£'000	£'000
	Non-HRA	168,854	172,230	202,249
	HRA	-7,739	-7,739	-7,739
	Total CFR	**158,115**	**164,491**	**194,510**

The year-on-year change in the CFR is due to the following:

Capital Financing Requirement	**2009-10**	2010-11	2011-12
	Estimate £'000	Estimate £'000	Estimate £'000
Balance B/F	**161,551**	165,854	172,230
Capital expenditure financed from borrowing (per 2.2)	**8,787**	11,031	34,930
Revenue provision for debt Redemption.	**-4,484**	**-4,655**	**-4,911**
Other items *(specify)*			
Balance C/F	**165,854**	**172,230**	**202,249**

4.3 In order to ensure that over the medium term net borrowing will only be for a capital purpose, the Council should make sure that net external borrowing does not, except in the short term, exceed the Capital Financing Requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

4.4 The Director of Corporate Resources will ensure that the Council does not have difficulties in meeting this requirement in 2009-10 or future financial years.

5. Incremental Impact of Capital Investment Decisions

5.1 This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax and Housing Rent levels. The incremental impact is calculated by comparing the total revenue budget requirement of the current approved capital programme with an equivalent calculation of the revenue budget requirement arising from the proposed capital programme.

No. 5	**Incremental Impact of Capital Investment Decisions**	**2009-10**	2010-11	2011-12
		Estimate £	Estimate £	Estimate £
	Band D Council Tax	**2.03**	8.73	13.40
	Average Weekly Housing Rents	**0.07**	0.12	0.16

6 Authorised Limit and Operational Boundary for External Debt

6.1 The Council has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise as a consequence of all the financial transactions of the Council and not just those arising from capital spending reflected in the CFR.

6.2 The **Authorised Limit** sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities. This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases. It is consistent with the Council's existing commitments, its proposals for capital expenditure and financing and its approved treasury management policy statement and practices.

6.3 The Authorised Limit has been set on the best estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements. The Limit is set by reference to the CFR as its major component, but with allowance made to enable for proactive treasury management activity to be undertaken. Provision has also been made to take account of potential cash flow volatility arising at the commencement of a new local authority.

6.4 The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

No. 6	**Authorised Limit for External Debt**	**2009-10**	2010-11	2011-12
		Estimate £m	Estimate £m	Estimate £m
	Borrowing	**360**	**360**	**360**
	Other Long-term Liabilities	**0**	0	0
	Total	**360**	**360**	**360**

6.5 The **Operational Boundary** links directly to the Council's estimates of the CFR and estimates of other cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

6.6 The Chief Financial Officer has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next meeting of the Cabinet and Council

No. 7	**Operational Boundary for External Debt**	**2009-10**	2010-11	2011-12
		Estimate £m	Estimate £m	Estimate £m
	Borrowing	**350**	**350**	**350**
	Other Long-term Liabilities	**0**	0	0
	Total	**350**	**350**	**350**

7. Adoption of the CIPFA Treasury Management Code:

7.1 This indicator demonstrates that the Council has adopted the principles of best practice. It is therefore recommended that the Council adopts the CIPFA Treasury Management Code along with its Treasury Strategy for 2009-10.

8. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

8.1 These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. This Council calculates these limits on a net interest paid basis (i.e. interest paid on fixed rate debt net of interest received on fixed rate investments).

8.2 The upper limit for variable rate exposure has been set to ensure that the Council is not exposed to interest rate rises which could adversely impact on the revenue budget. The limit allows for the use of variable rate debt to offset exposure to changes in short-term rates on investments

		2009-10	2010-11	2011-12
		Estimate %	Estimate %	Estimate %
No. 9	**Upper Limit for Fixed Interest Rate Exposure**	**100**	100	100
No. 10	**Upper Limit for Variable Rate Exposure**	**50**	50	50

8.3 The limits above provide the necessary flexibility within which decisions will be made for drawing down new loans on a fixed or variable rate basis; the decisions will ultimately be determined by expectations of anticipated interest rate movements as set out in the Council's treasury management strategy.

9 Maturity Structure of Fixed Rate borrowing

9.1 This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period, in particular in the course of the next ten years.

9.2 It is calculated as the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate. The maturity of borrowing is determined by reference to the earliest date on which the lender can require payment. The Limits have been set at their widest parameters to accommodate any debt rescheduling that may be felt necessary following the disaggregation of the Bedfordshire County Council debt portfolio to Central Bedfordshire.

No. 11	**Maturity structure of fixed rate borrowing**	**Lower Limit %**	**Upper Limit %**
	under 12 months	0	100
	12 months and within 24 months	0	100
	24 months and within 5 years	0	100
	5 years and within 10 years	0	100
	10 years and above	0	100

10. Upper Limit for total principal sums invested over 364 days

10.1 The purpose of this limit is to contain exposure to the possibility of loss that may arise as a result of the Council having to seek early repayment of the sums invested. It reflects the minimum level of Balances and Reserves that the Council may expect to hold over the medium term.

No. 12	**Upper Limit for total principal sums invested over 364 days**	**2009-10**	2010-11	2011-12
		Estimate £m	Estimate £m	Estimate £m
		20	**20**	**20**

APPENDIX B

Arlingclose's Forecast for Interest Rates (December 2008)

	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11
Official Bank Rate									
Upside risk							+0.25	+0.25	+0.25
Central case	**1.00**	**1.00**	**1.00**	**1.00**	**1.00**	**1.50**	**2.00**	**2.50**	**2.50**
Downside risk	-0.50	-0.75	-0.75	-0.75	-0.75	-0.50	-0.50	-0.50	-0.50
1-yr LIBID									
Upside risk									
Central case	**2.50**	**1.75**	**1.50**	**1.50**	**1.50**	**1.75**	**2.00**	**2.75**	**3.00**
Downside risk	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
5-yr gilt									
Upside risk									
Central case	**3.00**	**2.75**	**2.50**	**2.00**	**2.00**	**2.50**	**2.75**	**3.00**	**4.00**
Downside risk		-0.50	-0.50	-0.50	-0.50	-0.50			
10-yr gilt									
Upside risk									
Central case	**3.40**	**3.10**	**3.00**	**3.00**	**3.00**	**3.50**	**3.75**	**4.00**	**4.50**
Downside risk	-0.25	-0.25	-0.50	-0.50	-0.50	-0.50			
20-yr gilt									
Upside risk		+0.10	+0.10	+0.10	+0.10	+0.10			
Central case	**4.00**	**4.00**	**4.00**	**4.25**	**4.25**	**4.50**	**4.75**	**4.75**	**4.75**
Downside risk		-0.10	-0.10	-0.10	-0.10	-0.10			
50-yr gilt									
Upside risk	+0.10	+0.10	+0.10	+0.10	+0.10	+0.10	+0.10	+0.10	+0.10
Central case	**3.90**	**3.90**	**4.00**	**4.00**	**4.25**	**4.50**	**4.50**	**4.50**	**4.50**
Downside risk	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10

- The inflationary threats of 2008 turn into the deflationary reality of 2009. Central Banks under pressure to reduce rates decisively – even to zero or near-zero – to avoid the perils of a destructive and prolonged recession.
- The downturn in the UK gathers pace and the economy contracts for much of 2009. Prospects for Bank of England "Quantitative easing" increasingly likely.
- Pension, hedge and insurance fund values struggle and lead to enhanced demand for longer dated gilts.

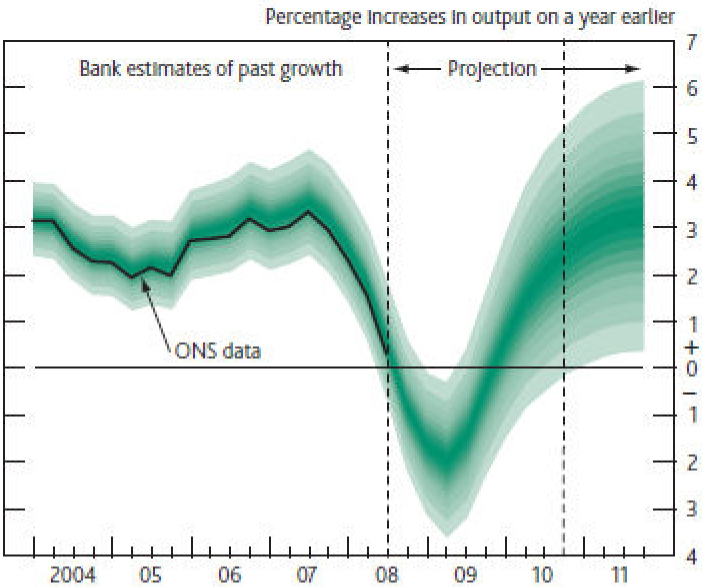
Underlying assumptions

- Despite central bank intervention to raise bank capital and improve liquidity, conditions in money and credit markets remain very difficult as banks' lending behaviour changes fundamentally.
- Consumer spending and business investment stall, hampered by the credit drought.
- Falling house prices compel households to review savings levels and repair balance sheets (where possible).
- Commodity prices continue to fall. CPI is projected to fall below the MPC's 1% lower threshold in 2009, providing some relief for the overstretched consumer, but eroding debt burdens more slowly.
- Fear of rising unemployment dampens confidence and any prospect of sizeable wage demands.

- UK public finances are in horrid shape and will worsen as the recession bites, resulting in a slew of gilt issuance in 2009. This will ultimately push gilt yields higher, although not aggressively so.
- Global growth and activity continue to weaken. The Federal Reserve has already cut rates to a range between 0% and 0.25% and has engaged in 'quantitative easing'. The ECB could bring rates down to 2% as European economies struggle with falling domestic and international demand.
- The Bank of England outlook for economic growth and inflation (as at November 2008) is shown below:

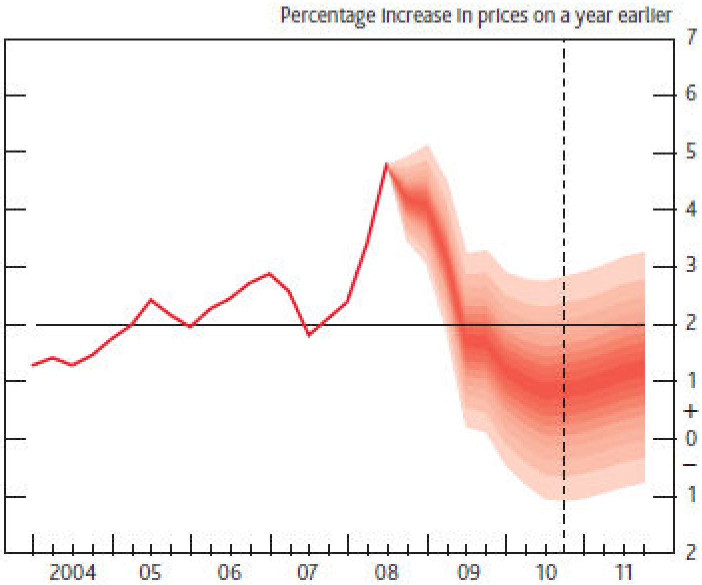
Projection for UK growth and inflation – source Bank of England's Inflation Report, November 2008

Chart 1 GDP projection based on market interest rate expectations



The fan chart depicts the probability of various outcomes for GDP growth. To the left of the first vertical dashed line, the distribution reflects the likelihood of revisions to the data over the past; to the right, it reflects uncertainty over the evolution of GDP growth in the future. If economic circumstances identical to today's were to prevail on 100 occasions, the MPC's best collective judgement is that the mature estimate of GDP would lie within the darkest central band on only 10 of those occasions. The fan chart is constructed so that outturns are also expected to lie within each pair of the lighter green areas on ten occasions. Consequently, GDP growth is expected to lie somewhere within the entire fan on 90 out of 100 occasions. The bands widen as the time horizon is extended, indicating the increasing uncertainty about outcomes. The second dashed line is drawn at the two-year point of the projection

Chart 2 CPI inflation projection based on market interest rate expectations



The fan chart depicts the probability of various outcomes for CPI inflation in the future. If economic circumstances identical to today's were to prevail on 100 occasions, the MPC's best collective judgement is that inflation over the subsequent three years would lie within the darkest central band on only 10 of those occasions. The fan chart is constructed so that outturns of inflation are also expected to lie within each pair of the lighter red areas on 10 occasions. Consequently, inflation is expected to lie somewhere within the entire fan chart on 90 out of 100 occasions. The bands widen as the time horizon is extended, indicating the increasing uncertainty about outcomes.

All graphs and text as sourced from the Bank of England Inflation Report, November 2008

Annual MRP Statement Appendix C

Background:

1. For many years local authorities have been required by Statute and associated Statutory Instruments to charge to the Revenue Account an annual provision for the repayment of debt associated with expenditure incurred on capital assets. This charge to the Revenue Account was referred to as the Minimum Revenue Provision (MRP).

2. In February 2008 the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [Statutory Instrument 2008/414] were approved by Parliament and became effective on 31 March 2008. These regulations replace the formula based method for calculating MRP which existed under previous regulations under the Local Government Act 2003. The new regulations require a local authority to determine each financial year an amount of MRP which it considers to be prudent. Linked to this new regulation, the Department of Communities and Local Government (DCLG) has produced Statutory Guidance which local authorities are required to follow, setting out what constitutes a prudent provision.

3. The DCLG Guidance recommends that before the start of the financial year, a statement of MRP policy for the forthcoming financial year is approved by the Full Council.

4. The broad aim of the Policy is to ensure that MRP is charged over a period that is reasonably commensurate with the period over which the capital expenditure which gave rise to the debt provides benefits. In the case of borrowing supported by Revenue Support Grant, the aim is that MRP is charged over a period reasonably commensurate with the period implicit in the determination of that grant. MRP is not required to be charged to the Housing Revenue Account. Where a local authority's overall CFR is £nil or a negative amount there is no requirement to charge MRP.

MRP Options:

5. Four options for prudent MRP provision are set out in the DCLG Guidance. Details of each are set out below with a summary set out in Table 1:

Option 1 – Regulatory Method:

6. This method replicates the position that would have existed under the previous Regulatory environment. MRP is charged at 4% of the Authority's underlying need to borrow for capital purposes; the Capital Financing Requirement (CFR). The formula includes an item known as "Adjustment A" which was intended to achieve neutrality between the CFR and the former Credit Ceiling which was used to calculate MRP prior to the introduction of the Prudential System on 1st April 2004. The formula also took into account any reductions possible related to commutation of capital related debt undertaken by central government.

7. All the predecessor authorities to Central Bedfordshire placed reliance on Adjustment A to minimize their calculations of MRP.

Option 2 – CFR Method:

8. This method simplifies the calculation of MRP by basing the charge solely on the authority's CFR but excludes the technical adjustments included in Option 1. The annual MRP charge is set at 4% of the non-housing CFR at the end of the preceding financial year.

9. The General Fund MRP charge for this method would be greater than that under Option 1 due to the effect of excluding the impact of Adjustment A.

Option 3 – Asset Life Method:

10. Under this method MRP is determined by the life of the asset for which the borrowing is undertaken. This can be calculated by either of the following methods:

    (a) Equal Instalments: where the principal repayment made is the same in each year, or

    (b) Annuity: where the principal repayments increase over the life of the asset

11. MRP commences in the financial year following that in which the expenditure is incurred or, in the year following that in which the relevant asset becomes operational. This enables an MRP "holiday"

to be taken in relation to assets which take more than one year to be completed before they become operational.

12. The estimated life of the asset will be determined in the year that MRP commences and will not be subsequently revised. However, additional repayments can be made in any year which will reduce the level of payments in subsequent years.

13. If no life can be reasonably attributed to an asset, such as freehold land, the life is taken to be a maximum of 50 years. In the case of freehold land on which a building or other structure is constructed, the life of the land will be treated as equal to that of the structure, where this would exceed 50 years.

14. In instances where central government permits revenue expenditure to be capitalised, the Statutory Guidance sets out the number of years over which the charge to revenue must be made.

Option 4 - Depreciation Method:

15. The deprecation method is similar to that under Option 3 but MRP will is equal to the depreciation provision required in accordance with proper accounting practices to be charged to the Income and Expenditure account

Conditions of Use:

16. The DCLG Guidance puts the following conditions on the use of the four options:

Options 1 and 2 can be used on all capital expenditure incurred before 1 April 2008 and on Supported Capital Expenditure on or after that date.

Options 3 and 4 are considered prudent options for Unsupported Capital Expenditure on or after 1 April 2008.These options can also be used for Supported Capital Expenditure whenever incurred.

MRP Policy for 2009/10:

17. It is proposed that for 2009/10 the Council adopts Option 1 for Supported Borrowing and Method 3 for Unsupported Borrowing.

Table 1

MRP under DCLG 2008 Regulations

MRP Options	1 Regulatory Method	2 CFR Method	3 Asset Life Method	4 Depreciation Method
Classifications of Capital Expenditure impacting on the CFR	Capital expenditure incurred before 1 April 2008			
	Supported Capital expenditure incurred after 1 April 2008		Unsupported Capital expenditure incurred after 1 April 2008	
			Expenditure capitalised by virtue of a Direction under s16(2)(b) of the Local Government Act 2003	
MRP Basis	Former regulations 28 and 29	4% of Non-Housing CFR	Equal Annual Instalments of Principal or Annuity	Depreciation
Aspects of MRP charges	CFR excludes element attributable to Unsupported Capital Expenditure		EIP commences when asset operational	Depreciation MRP commences when asset operational
			Freehold land 50 years.	Depreciation MRP ceases when CFR component is £Nil
			Freehold land with structure >50 years	Depreciation MRP not adjusted for capital receipt
			Capitalisation periods	Depreciation MRP based on proportion of asset financed from "borrowing".