Taunton Deane Borough Council

Executive – 16 March 2011

Treasury Management Strategy Statement and Investment Strategy

Report of the Strategic Finance Officer
(This matter is the responsibility of Executive Councillor Williams – Leader of the Council)

1. Executive Summary

- Council debt at the time of issue of report is £14.5m, outstanding investments are £16.2m;
- Short-term interest rates currently at 0.5% and are forecast to rise to 0.75% in the third quarter of the year and 1.0% in the fourth quarter of 2011;
- Long-term rates more stable at 4.25 -4.75% (50yrs) for this financial year;
- Interest rates at historic all time low levels.

2. Background

2.1 The purpose of this Treasury Management Strategy Statement and Investment Strategy (TMSS) is to approve:-

- The Treasury Management Strategy for 2011/2012 (Borrowing and Debt Rescheduling);
- The Prudential Indicators;
- The Minimum Revenue Provision Statement; and
- Use of Specified and Non-Specified Investments.

3. Treasury Management Strategy Statement (TMSS) and Investment Strategy

3.1 Appendix 1 gives the full TMSS.

4. Finance Comments

4.1 This is a finance report and there are no further comments to make.

5. Legal Comments

5.1 There are no legal implications in this report.

6. Links to Corporate Aims

6.1 The TMSS supports the funding of projects as well as the general fund, which in turn support the Corporate Aims.

7. Equalities Impact

7.1 After initial screening no Equality Impacts were identified for any specific group.

8. Partnership Implications

8.1 Southwest One performs the treasury management function on behalf of Taunton Deane Borough Council. Southwest One will adhere to this strategy.

9. Recommendations

9.1.1 That the Executive approves the proposed Treasury Management Strategies outlined in this report.

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IMPORTANT – PLEASE NOTE:
In order for this item to be debated in the most efficient manner at Executive, Members who have queries with any aspect of the report are requested to contact the officer named above before the meeting.

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Appendix 1

Taunton Deane BC
Treasury Management Strategy Statement
and Investment Strategy 2011/12 to 2013/14

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Appendices

1. Background

Treasury Management Strategy Statement
and Investment Strategy 2011/12 to 2013/14

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 local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators on an annual basis. The TMSS also incorporates the Investment Strategy as required under the CLG's Investment Guidance.

1.2. CIPFA has defined Treasury Management as:

"the management of the organisation's investments and 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 is responsible for its treasury decisions and activity. No treasury management activity is without risk. The successful identification, monitoring and control of risk are integral element to treasury management activities and include Credit and Counterparty Risk, Liquidity Risk, Market or Interest Rate Risk, Refinancing Risk and Legal and Regulatory Risk.

1.4. The strategy takes into account the impact of the Council's Revenue Budget and Capital Programme on the Balance Sheet position, the current and projected Treasury position (Appendix A), the Prudential Indicators and the outlook for interest rates (Appendix B).

1.5. The purpose of this TMSS is to approve:

- Treasury Management Strategy for 2011-12 (Borrowing and Debt Rescheduling - Section 4, Investments - Section 5)
- Prudential Indicators – (NB: the Authorised Limit is a statutory limit)
- MRP Statement – Section 8
- Use of Specified and Non-Specified Investments – Appendices C & D

1.6. As per requirements of the Prudential Code, the Council has adopted the CIPFA Treasury Management Code. The Council has incorporated the changes from the revised CIPFA Code of Practice (November 2009) into its treasury policies, procedures and practices.[1]

1.7. All treasury activity will comply with relevant statute, guidance and accounting standards.

2. Balance Sheet and Treasury Position

2.1. The underlying need to borrow for capital purposes, as measured by the Capital Financing Requirement (CFR)[2], together with Balances and Reserves, are the core drivers of Treasury Management Activity. The estimates, based on the current Revenue Budget and Capital Programmes, are:

	31/03/2011 Estimate £m	31/03/2012 Estimate £m	31/03/2013 Estimate £m	31/03/2014 Estimate £m
General Fund CFR	12.260	12.015	12.796	13.864
HRA CFR	14.451	14.451	**101.651	**101.651
Total CFR	26.711	26.466	114.447	115.515
Less: Existing Profile of Borrowing and Other Long Term Liabilities	14.5	9.0	9.0	9.0
Cumulative Maximum External Borrowing Requirement	**12.211**	**17.466**	**105.447**	**106.515**
Balances & Reserves	**8.35**	**5.028**	**3.668**	**-0.928**
Cumulative Net Borrowing Requirement/(Investments)	**3.861**	**12.438**	**101.779**	**107.443**

****The HRA CFR figures for 31/3/2013 and 31/3/2014 include the indicative additional borrowing of £87.2m the Council will have to self-finance as a result of the abolition of the Housing Subsidy system. This additional borrowing is also reflected in other projections within this document.

2.2. The Council's level of physical debt and investments is linked to these components of the Balance Sheet. The current portfolio position is set out at **Appendix A**. Market conditions, interest rate expectations and credit risk considerations will influence the Council's strategy in determining the borrowing and investment activity against the underlying Balance Sheet position. The Council will ensure that net physical external borrowing (i.e. net of investments) will not exceed the CFR other than for short term cash flow requirements.

Estimates of Capital Expenditure:

2.3. It is a requirement of the Prudential Code to ensure that 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.

Capital Expenditure	2010/11 Approved £m	2010/11 Revised £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
Non-HRA	2.852	6.689	**1.421**	1.910	1.875
HRA	6.231	6.231	**4.300**	91.599	91.22
Total	**9.083**	**12.920**	**5.721**	**93.509**	**93.095**

2.4. Capital expenditure is expected to be financed as follows:

Capital Financing	2010/11 Approved £m	2010/11 Revised £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
Capital receipts	0.232	0.297	**0.487**	0.276	0.100
Government Grants	2.181	2.181	**0.259**	0.259	0.259
Major Repairs Allowance	3.785	3.785	**3.867**	0.000	0.000
Revenue contributions	2.222	2.733	**1.108**	0.781	0.151
Total Financing	8.420	8.996	**5.721**	1.316	0.510
Supported borrowing	620	620	**0**	0	0
Unsupported borrowing	2.530	3.304	**5.721**	88.243	88.550
Total Funding	3.150	3.924	**0**	88.243	88.550
Total Financing and Funding	**11.570**	**12.920**	**5.721**	**89.559**	**89.060**

Incremental Impact of Capital Investment Decisions:

2.5. As an indicator of affordability the table below 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.

Incremental Impact of Capital Investment Decisions	2010/11 Approved £	2011/12 Estimate £	2012/13 Estimate £	2013/14 Estimate £
Increase in Band D Council Tax	2.90	**-0.84**	0.00	0.16
Increase in Average Weekly Housing Rents	0.00	**0.00**	0.00	0.00

2.6. **Reform to the Council Housing Subsidy System**: CLG consulted on proposals to reform the council housing subsidy system in July 2010. The consultation proposed a removal of the subsidy system by offering a one-off reallocation of debt. Details of the new system have been introduced in the Localism Bill to enable the new system to start in 2012, subject to the enabling legislation being passed in 2011.

This will require the Council to fund the amount (£87m) owed in the medium term through internal resources and/or external borrowing. The Council has the option of borrowing from the PWLB or the market. The type of loans taken will be decided on in discussions with the Housing department and the councils' Treasury Advisors.

2.7. The estimate for interest payments in 2011/12 is £650k and for interest receipts is £156k. Interest payments are estimated on the existing loans portfolio of £14.5m and do not include any costs related to HRA subsidy reform borrowing that may be undertaken in advance of 01/4/2012. The ratio of financing costs to the Council's net revenue stream 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 ratio is based on costs net of investment income.

Ratio of Financing Costs to Net Revenue Stream	2010/11 Approved %	2011/12 Estimate %	2012/13 Estimate %	2013/14 Estimate %
Non-HRA	1.08	**1.32**	1.70	1.75
HRA	1.81	**2.28**	2.17	2.07
Total	**1.52**	**1.95**	**2.02**	**1.97**

3. Borrowing and Rescheduling Strategy

3.1. The Council's balance of Actual External Debt at 31/03/10 (gross borrowing plus other long-term liabilities) is shown in Appendix A. This Prudential Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

3.2. The **Authorised Limit** sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) and is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

Authorised Limit for External Debt	2010/11 Approved £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m
Borrowing	40.0	**140.0**	140.0	140.0
Other Long-term Liabilities	0.0	**0.0**	0.0	0.0
Total	**40.0**	**140.0**	**140.0**	**140.0**

3.3. The **Operational Boundary** links directly to the Council's estimates of the CFR and estimates of other cashflow 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.

Operational Boundary for External Debt	2010/11 Approved £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m

Borrowing	30.0	**130.0**	130.0	130.0
Other Long-term Liabilities	0.0	**0.0**	0.0	0.0
Total	**30.0**	**130.0**	**130.0**	**130.0**

3.4 The s151 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 Council

3.4. In conjunction with advice from its treasury advisor, Arlingclose Ltd, the Council will keep under review the following borrowing options:

- PWLB loans
- Borrowing from other local authorities
- Borrowing from institutions such as the European Investment Bank and directly from Commercial Banks
- Borrowing from the Money Markets
- Local authority stock issues
- Local authority bills
- Structured finance

3.5. Notwithstanding the issuance of Circular 147 on 20th October following the CSR announcement which increases the cost of new local authority fixed rate loans to 1% above the cost of the Government's borrowing, the PWLB remains an attractive source of borrowing, given the transparency and control that its facilities continue to provide. The types of PWLB borrowing that are considered appropriate for a low interest rate environment are:

- Variable rate borrowing
- Medium-term Equal Instalments of Principal (EIP) or Annuity Loans
- Long-term Maturity loans, where affordable

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 and maintaining stability. The differential between debt costs and investment earnings, despite long term borrowing rates being at low levels, remains acute and this is expected to remain a feature during 2011/12. The "cost of carry" associated with medium- and long-term borrowing compared to temporary investment returns means that new fixed rate borrowing could entail additional short-term costs. The use of internal resources in lieu of borrowing may again, in 2011/12, be the most cost effective means of financing capital expenditure.

3.6. PWLB variable rates are expected to remain low as the Bank Rate is maintained at historically low levels for an extended period. Exposure to variable interest rates will be kept under regular review. Each time the spread between long-term rates and variable rates narrows by 0.50%, this will trigger a formal review point and options will be considered in conjunction with the Authority's Treasury Advisor and decisions taken on whether to retain the same exposure or change from variable to fixed rate debt.

3.7. The Council has a £3.0m loan which is a LOBO loan (Lender's Options Borrower's Option) which will be in its call period in 2011/12. In the event that the lender exercises the option to change the rate or terms of the loan, the Council will consider the terms being provided and also repayment of the loan without penalty. The Council may utilise cash resources for repayment or may consider replacing the loan(s) by borrowing from the PWLB. The default response will however be early repayment without penalty.

3.9 The Council will keep open the option to borrow £87.2m in advance of April 2012. This will allow TDBC to have the required sum within the bank to pay CLG in respect of the Housing Reform. Any borrowing will be done following advice from our Treasury Advisors. Investment balances are therefore likely to be higher by this amount for a period of up to 12 months before expenditure is incurred.

3.10 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.

As opportunities arise, they will be identified by Arlingclose and discussed with the Council's officers.

3.11 Borrowing and rescheduling activity will be reported to the Executive.

3.12 The following Prudential Indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. 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.

The Council's existing level of fixed interest rate exposure is 100% and variable rate exposure is 0%.

	Existing level at 31/03/10 %	**2010/11 Approved £m or %**	**2010/11 Revised £m or %**	**2011/12 Estimate £m or %**	**2012/13 Estimate £m or %**	**2013/14 Estimate £m or %**
Upper Limit for Fixed Interest Rate Exposure	85	100	100	**100**	100	100
Upper Limit for Variable Interest Rate Exposure	15	50	50	**50**	50	50

3.13. The Council will also limit and monitor large concentrations of fixed rate debt needing to be replaced. Limits in the following table are intended to control excessive exposures to volatility in interest rates when refinancing maturing debt.

Maturity structure of fixed rate borrowing	Existing level at 31/01/ 2011 %	Lower Limit for 2011/12 %	Upper Limit for 2011/12 %
under 12 months	58%	0%	50%
12 months and within 24 months		0%	50%
24 months and within 5 years	14%	0%	50%
5 years and within 10 years		0%	50%
10 years and within 20 years		0%	100%
20 years and within 30 years		0%	100%
30 years and within 40 years		0%	100%
40 years and within 50 years	28%	0%	100%
50 years and above		0%	100%

4. Investment Policy and Strategy

4.1. Guidance from CLG on Local Government Investments in England requires that an Annual Investment Strategy (AIS) be set.

4.2. 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.

4.3. Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the CLG Guidance. Potential instruments for the Council's use within its investment strategy are contained in Appendices C and D. The s151 Officer, 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.

4.4. Changes to investment strategy for 2011/12 include:

- AAA-rated Variable Net Asset Value (VNAV) Money Market Funds
- T-Bills
- Local Authority Bills
- Term deposits in Sweden
- Maximum duration for new term deposits 2 years

4.5. As identified in Section 3.9 of this TMSS, the Council's investments are likely to include £87.2m borrowed in advance of spending needs. Investment balances are therefore likely to be higher by this amount for a period of up to 12 months before expenditure is incurred.

The management of risks, including the risk of loss of the borrowed capital are identical to all forms of investment as set out in this strategy. The risk associated with interest rate changes are based on the Interest Rate forecast at **Appendix C** and the current "cost of carry".

4.6. The Council's current level of investments is presented at Appendix A.

4.7. The Council's in-house investments are made with reference to the outlook for the UK Bank Rate and money market rates.

4.8. In any period of significant stress in the markets, the default position is for investments to be made with the Debt Management Office or UK Treasury Bills. (The rates of interest from the DMADF are below equivalent money market rates, but the returns are an acceptable trade-off for the guarantee that the Council's capital is secure.)

4.9. The Council selects countries and the institutions within them (see Appendix C), for the counterparty list after analysis and careful monitoring of:

- Credit Ratings (minimum long-term A+ for counterparties; AA+ for countries)
- Credit Default Swaps (where quoted)
- GDP; Net Debt as a Percentage of GDP
- Sovereign Support Mechanisms/potential support from a well-resourced parent institution
- Share Prices (where quoted)
- Macro-economic indicators
- Corporate developments, news and articles , market sentiment.

4.10. The Council and its Treasury Advisors, Arlingclose, will continue to analyse and monitor these indicators and credit developments on a regular basis and respond as necessary to ensure security of the capital sums invested.

4.11. The UK Bank Rate has been maintained at 0.5% since March 2009, and is anticipated to remain at low levels throughout 2011/12. Short-term money market rates are likely to remain at very low levels for an extended period which will have a significant impact on investment income.

4.12. To protect against a lower for longer prolonged period of low interest rates and to provide certainty of income, 2-year deposits and longer-term secure investments will be actively considered within the limits the Council has set for Non-Specified Investments (see Appendix D). The longer-term investments will be likely to include:

- Term Deposits with counterparties rated at least A+ (or equivalent)
- Supranational Bonds (bonds issued by multilateral development banks): Even at the lower yields likely to be in force, the return on these bonds will provide certainty of income against an outlook of low official interest rates.

4.13. The Council has placed an upper limit for principal sums invested for over 364 days, as required by the Prudential Code. 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.

4.14.

No. 12	Upper Limit for total principal sums invested over 364 days [3]	2010/11 Approved £m/%	2010/11 Revised £m/%	2011/12 Estimate £m/%	2012/13 Estimate £m/%	2013/14 Estimate £m/%
	Whichever is the higher	2.0	3.5	3.5 or 20%	3.5 or 20%	3.5 or 20%

4.15. Collective Investment Schemes (Pooled Funds):

The Council has evaluated the use of Pooled Funds and determined the appropriateness of their use within the investment portfolio. Pooled funds enable the Council to diversify the assets and the underlying risk in the investment portfolio and provide the potential for enhanced returns.

4.16. Investments in pooled funds will be undertaken with advice from Arlingclose. The Council's currently invests in constant value Money Market Funds.

5. Outlook for Interest Rates

5.1 The economic interest rate outlook provided by the Council's treasury advisor, Arlingclose Ltd, is attached at Appendix B. The Council will reappraise its strategy from time to time and, if needs be, realign it with evolving market conditions and expectations for future interest rates.

6. Balanced Budget Requirement

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

7. 2011/12 MRP Statement

7.1. The Local Authorities (Capital Finance and Accounting)(England)(Amendment) Regulations 2008 (SI 2008/414) place a duty on local authorities to make a prudent provision for debt redemption. Guidance on Minimum Revenue Provision has been issued by the Secretary of State and local authorities are required to "have regard" to such Guidance under section 21(1A) of the Local Government Act 2003.

7.2. The four MRP options available are:

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

NB This does not preclude other prudent methods.

7.3. MRP in 2011/12: Options 1 and 2 may be used only for supported expenditure. Methods of making prudent provision for self financed expenditure include Options 3 and 4 (which may also be used for supported expenditure if the Council chooses).

7.4. The MRP Statement will be submitted to Council before the start of the 2011/12 financial year. If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement should be put to Council at that time.

7.5. The Council will apply Option 2 in respect of supported capital expenditure and Option 3 in respect of unsupported capital expenditure.

8. Monitoring and Reporting on the Treasury Outturn and Prudential Indicators

Treasury activity is monitored and reported internally to s151 Officer. The Prudential Indicators will be monitored through the year by the s151 officer and reported as below :

The s151 officer will report to the Executive on treasury management activity / performance and Performance Indicators as follows:
(a) Half yearly against the strategy approved for the year.
(b) The Council will produce an outturn report on its treasury activity no later than 30th September after the financial year end.
(c) Executive will be responsible for the scrutiny of treasury management activity and practices.

9. Other Items

Training

CIPFA's Code of Practice requires the s151 officer to ensure 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.

Reviewing and addressing training needs:
Taunton Deane Borough Council trains new members in its finances including treasury management. Refresher financial training is offered which includes treasury management. Our treasury advisors also present to members at Members Briefings. Council staff (including SWOne secondees) attend regular treasury management training.

Investment Consultants

The CLG's Guidance on local government investments recommend that the Investment Strategy should state:

- Whether and, if so, how the authority uses external contractors offering information, advice or assistance relating to investment and
- How the quality of any such service is controlled.

Taunton Deane Borough Council uses the advice of external contractors. This advice is used to maximise returns on investments whilst retaining certainty over the sum invested. It is also used to ensure that any borrowing is at the best rate available.

The external consultants meet regularly with the s151 officer to review treasury management activities including their advice.

APPENDIX A

EXISTING PORTFOLIO PROJECTED FORWARD

	31 Mar 10 Actual Portfolio £m	%	31 Mar 11 Estimate £m	31 Mar 12 Estimate £m	31 Mar 13 Estimate £m	31 Mar 14 Estimate £m
External Borrowing:						
Fixed Rate – PWLB	6.0		6.0	6.0	93.2	93.2
Fixed Rate – Market	3.0		8.5	8.5	8.5	8.5
Variable Rate – PWLB	6.0					
Variable Rate – Market						
Total External Borrowing	15.0		14.5	14.5	101.7	101.7
Existing long-term liabilities	0.0		0.0	0.0	0.0	0.0
Other Long Term Liabilities:						
- PFI	0		0	0	0	0
- Finance Leases	0		0	0	0	0
- Operating Leases*	0		0	0	0	0
Total Gross External Debt	15.0		14.5	14.5	101.7	101.7
Investments:						
Managed in-house						
- Short-term monies (Deposits/ monies on call /MMFs)	11.7		8.0	8.0	8.0	8.0
- Long-term investments						
Managed externally						
- By Fund Managers						
- Pooled Funds *(please list)*						
Total Investments	11.7		8.0	8.0	8.0	8.06
(Net Borrowing Position)/ Net Investment position	(3.3)		(6.5)	(6.5)	(93.7)	(93.7)

*Operating Leases reclassified as Finance Leases as a result of IFRS

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APPENDIX B

Arlingclose's Economic and Interest Rate Forecast

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Official Bank Rate													
Upside risk	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	**0.50**	**0.50**	**0.75**	**1.00**	**1.25**	**1.50**	**2.00**	**2.50**	**2.75**	**2.75**	**3.00**	**3.00**	**3.00**
Downside risk	-	-	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50
1-yr LIBID													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	**1.65**	**1.90**	**2.15**	**2.40**	**2.50**	**2.50**	**2.75**	**3.00**	**3.25**	**3.50**	**3.50**	**3.50**	**3.50**
Downside risk	- 0.25	- 0.25	- 0.25	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50	- 0.50
5-yr gilt													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	**2.75**	**3.00**	**3.25**	**3.50**	**3.75**	**4.00**	**4.00**	**4.00**	**4.00**	**4.00**	**4.25**	**4.25**	**4.00**
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
10-yr gilt													
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	0.50
Central case	**3.90**	**4.00**	**4.10**	**4.25**	**4.50**	**4.75**	**4.75**	**4.75**	**4.75**	**4.75**	**5.00**	**5.00**	**4.75**
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
20-yr gilt													
Upside risk	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	**4.50**	**4.75**	**5.00**	**5.00**	**5.00**	**5.00**	**5.00**	**5.00**	**5.00**	**5.00**	**5.25**	**5.25**	**5.00**
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25
50-yr gilt													
Upside risk	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	**4.25**	**4.50**	**4.75**	**4.75**	**4.75**	**4.75**	**4.50**	**4.50**	**4.50**	**4.50**	**4.75**	**4.75**	**4.50**
Downside risk	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25	- 0.25

- The recovery in growth is likely to be slow and uneven.
- The initial reaction to the CSR is positive, but implementation risks remain.
- The path of base rates reflects the fragility of the recovery and the significantly greater fiscal tightening of the emergency budget. With growth and underlying inflation likely to remain subdued, the Bank will stick to its lower for longer stance on policy rates.
- Uncertainty surrounding Eurozone sovereign debt and the risk of contagion will remain a driver of global credit market sentiment.

Underlying assumptions:

- The framework and targets announced in the Comprehensive Spending Review (CSR) to reduce the budget deficit and government debt will be put to the test; meeting the 2010 borrowing target of £149bn will be crucial to the gilt market's confidence in the credibility of the deficit reduction plans.
- Despite Money Supply being weak and growth prospects remaining subdued, the MPC has gravitated towards increasing rates in the new year as global inflation continues to rise along with household inflation.
- Consumer Price Inflation is stubbornly above 3% and is likely to spike above 4% in the first quarter of 2011 as a result of VAT, Utilities and Rail Fares.
- Unemployment remains near a 16 year high, at just over 2.5 Million, and is set to increase as the Public Sector shrinks. Meanwhile employment is growing but this is mainly due to part time work, leaving many with reduced income.

- Recently announced Basel III capital/liquidity rules and extended timescales are positive for banks. Restructuring of UK banks' balance sheets is ongoing and expected to take a long time to complete. This will be a pre-condition for normalisation of credit conditions and bank lending.
- Mortgage repayment, a reduction in net consumer credit and weak consumer confidence are consistent with lower consumption and therefore the outlook for growth.
- The US Federal Reserve downgraded its outlook for US growth; the Fed is concerned enough to signal further QE through asset purchases. Industrial production and growth in the Chinese economy are showing signs of slowing. Both have implications for the global economy.

APPENDIX C

Specified and Non Specified Investments

Specified Investments identified for use by the Council

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

- is sterling denominated
- has a maximum maturity of 1 year
- meets the "high credit quality" as determined by the Council or is made with the UK government or is made with a local authority in England, Wales, Scotland or Northern Ireland or a parish or community council.
- 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).

"Specified" Investments identified for the Council's use are:

- Deposits in the DMO's Debt Management Account Deposit Facility
- Deposits with UK local authorities
- Deposits with banks and building societies
- *Certificates of deposit with banks and building societies
- *Gilts: (bonds issued by the UK government)
- *Bonds issued by multilateral development banks
- Treasury-Bills (T-Bills)
- Local Authority Bills (LA Bills)
- AAA-rated Money Market Funds with a Constant Net Asset Value (CNAV)
- AAA-rated Money Market Funds with a Variable Net Asset Value (VNAV)
- Other Money Market Funds and Collective Investment Schemes– i.e. credit rated funds which meet the definition of a collective investment scheme as defined in SI 2004 No 534 and SI 2007 No 573.

1. ** Investments in these instruments will be on advice from the Council's treasury advisor.*
2. *The use of the above instruments by the Council's fund manager(s) will be by reference to the fund guidelines contained in the agreement between the Council and the individual manager.*

For credit rated counterparties, the minimum criteria will be the lowest equivalent short-term and long-term ratings assigned by Fitch, Moody's and Standard & Poor's (where assigned).

Long-term minimum: A+(Fitch); A1 (Moody's;) A+ (S&P)
Short-term minimum: F1 (Fitch); P-1 (Moody's); A-1 (S&P)

The Council will also take into account information on corporate developments of and market sentiment towards investment counterparties.

New specified investments will be made within the following limits:

Instrument	**Country/ Domicile**	**Counterparty**	**Maximum Counterparty Limits %/£m**	***E.g.***
Term Deposits	UK	DMADF, DMO	No limit	
Term Deposits/Call Accounts	UK	Other UK Local Authorities	No limit	
Term Deposits/Call Accounts	UK	Counterparties rated at least A+ Long Term and F1 Short Term (or equivalent)		
Term Deposits/Call Accounts	Non-UK	Counterparties rated at least A+ Long Term and F1 Short Term (or equivalent) in select countries with a Sovereign Rating of at least AA+		
Gilts	UK	DMO	No limit	
T-Bills	UK	DMO	No limit	
LA-Bills	UK	Other UK Local Authorities	No limit	
Bonds issued by multilateral development banks		(For example, European Investment Bank/Council of Europe, Inter American Development Bank)		*EIB; CoE; IADB Bonds*
AAA-rated Money Market Funds	UK/Ireland/ Luxembourg domiciled	CNAV MMFs VNAV MMFs (where there is greater than 12 month history of a consistent £1 Net Asset Value)		*Standard Life; Goldman Sachs; Prime Rate; RBS; Ignis etc.* *Aviva VNAV MMF* *Investec Liquidity Fund*
Other MMFs and CIS	UK/Ireland/ Luxembourg domiciled	Pooled funds which meet the definition of a Collective Investment Scheme per SI 2004 No 534 and subsequent amendments		*Payden & Rygel; Investec Short Bond Fund*

NB Any existing deposits outside of the current criteria will be reinvested with the above criteria on maturity.

NB

Non-UK Banks *- These should be restricted to a maximum exposure of 25-30% per country. This means that effectively all your authority's investments can be made with non-UK institutions should you wish, but it limits the risk of over-exposure to any one country.*

MMFs *- We emphasise diversification for all investments including MMFs. We advise that, as far as is practicable, clients spread their investments in Money Market Funds between two funds or more.*

***Group Limits** - For institutions within a banking group, we advise a limit of 1.5 times the individual limit of a single bank within that group.*

Instrument	Country/ Domicile	Counterparty	Maximum Counterparty Limit £m/%	Maximum Group Limit (if applicable) £m
Term Deposits/Call Accounts	UK	Santander UK Plc (Banco Santander Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	Bank of Scotland (Lloyds Banking Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	Lloyds TSB (Lloyds Banking Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	Barclays Bank Plc	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	Clydesdale Bank (National Australia Bank Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	HSBC Bank Plc	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	Nationwide Building Society	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	NatWest (RBS Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	Royal Bank of Scotland (RBS Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	UK	Standard Chartered Bank	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Australia	Australia and NZ Banking Group	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Australia	Commonwealth Bank of Australia	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Australia	National Australia Bank Ltd (National Australia Bank Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Australia	Westpac Banking Corp	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Canada	Bank of Montreal	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Canada	Bank of Nova Scotia	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Canada	Canadian Imperial Bank of Commerce	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Canada	Royal Bank of Canada	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Canada	Toronto-Dominion Bank	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Finland	Nordea Bank Finland	3.5m or 20%	5.25m or 20%

Term Deposits/Call Accounts	France	BNP Paribas	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	France	Credit Agricole CIB (Credit Agricole Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	France	Credit Agricole SA (Credit Agricole Group)	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	France	Société Générale	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Germany	Deutsche Bank AG	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Netherlands	ING Bank NV	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Netherlands	Rabobank	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Sweden	Svenska Handelsbanken	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	Switzerland	Credit Suisse	3.5m or 20%	5.25m or 20%
Term Deposits/Call Accounts	US	JP Morgan	3.5m or 20%	5.25m or 20%

Please note this list could change if, for example, a counterparty/country is upgraded, and meets our other creditworthiness tools. Alternatively if a counterparty is downgraded, this list may be shortened.

APPENDIX D

Non-Specified Investments determined for use by the Council

Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the Council's use: *(please amend the table below as applicable – we encourage you to discuss with Arlingclose the instruments and limits appropriate to your Council's strategy.)*

	In-house use	Use by fund managers	Maximum maturity	Max limit	Capital expenditure?	*E.g.*
▪ Deposits with banks and building societies ▪ CDs with banks and building societies	✓ ✓	✓		£3.5m	No	
▪ Gilts ▪ Bonds issued by multilateral development banks ▪ Bonds issued by financial institutions guaranteed by the UK government ▪ Sterling denominated bonds by non-UK sovereign governments	✓ (on advice from treasury advisor)	✓		£3.5m	No	*EIB Bonds, Council of Europe Bonds etc.*
Money Market Funds and Collective Investment Schemes, which are/ are not credit rated	✓ (on advice from treasury advisor)	✓			No	*Investec Target Return Fund; Elite Charteris Premium Income Fund*

1. In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty.

2. The use of the above instruments by the Council's fund manager(s) will be by reference to the fund guidelines contained in the agreement between the Council and the individual manager.