Appendix E

Treasury Management Strategy Statement and Investment Strategy 2010 to 2013

1. BACKGROUND

1.1 The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in the Public Services (the "CIPFA TM Code") requires local authorities to determine their Treasury Management Strategy Statement (TMSS). This statement also incorporates the Investment Strategy. Together, these cover the financing and investment strategy for the forthcoming financial year.

1.2 In response to the financial crisis in 2008 and the collapse of the Icelandic banks, in November 2009 CIPFA issued a revised Treasury Management Code of Practice and also a revised Prudential Code. Key changes relating to Member scrutiny of the Treasury Management Strategy include nominating a responsible body to oversee the treasury management function and the requirement to issue, as a minimum, a mid-year report reviewing treasury activity.

1.3 Herefordshire council's treasury management is subject to scrutiny by Cabinet and since September 2009 the treasury team have issued quarterly reports.

1.4 CIPFA defines 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."

1.5 The purpose of this Treasury Management Strategy Statement is to approve:

- Treasury Management Strategy for 2010-11 (Borrowing - Section 4, Debt Rescheduling - Section 5, Investments - Section 6)
- Prudential Indicators – Appendix 2
- MRP Statement – Section 8
- Use of Specified and Non-Specified Investments – Appendix 4

2. CURRENT TREASURY POSITION

2.1 The council's treasury portfolio position as at 31st December 2009 is as follows: -

DEBT POSITION	**Principal (£)**	**Borrowing Rate (%)**
Public Works Loan Board	103,595,378	4.47
Market Debt *	12,000,000	4.50
Total Debt	**115,595,378**	**4.48**

The estimated Borrowing Requirement 2010/11 – supported borrowing approvals of approximately £13.21 million, plus the potential for an additional £18.50 million unsupported borrowing under the Prudential Code (which includes slippage from previous year). In addition refinancing of maturing debt of £267,698 in the year will be required, plus there is the possibility that the market debt of £12,000,000 will require refinancing.

* The Market debt refers to two LOBO (Lender Option Borrower Option) loans of £6 million each (see 4.12).

INVESTMENT POSITION	**Principal (£)**	**Rate of Return (%)**
Total Investments (Internally Managed)	**26,110,000**	**0.81**

3. OUTLOOK FOR INTEREST RATES

3.1 The economic interest rate outlook provided by the council's treasury adviser, is attached at Appendix 3. Financial markets remain reasonably volatile. This volatility provides opportunities for active treasury management. The council will regularly reappraise its strategy and, realign it with changing market conditions and expectations for future interest rates.

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) – see Appendix 1. The CFR represents the cumulative capital expenditure of the local authority that has not been financed. To ensure that this expenditure will ultimately be financed, local authorities are required to make a Minimum Revenue Provision (MRP) for debt redemption from within the revenue budget each year.

4.2 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 in turn produce an increased requirement to charge MRP in the Revenue Account.

4.3 Actual external borrowing may be greater or less than the CFR, but in accordance with the Prudential Code, the council will ensure that net external borrowing (borrowing net of investments) does not, except in the short term, exceed the CFR in the preceding year plus the estimates of any additional CFR for the current and next two financial years.

4.4 The council's strategy is 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.

4.5 In conjunction with advice from its treasury advisor, 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).

The outlook for borrowing rates:

4.6 The differential between investment earnings and debt costs, despite long term borrowing rates being around historically low levels, is expected to remain a feature during 2010/11. During the current financial year the use of internal resources in lieu of borrowing has been the most cost effective means of financing capital expenditure but, at some stage, internal resources will become depleted and require topping up. This will be closely monitored.

4.7 PWLB variable rates have fallen below 1%. They are expected to remain low as the Bank Rate is maintained at historically low levels to support the economy. With interest rates remaining lower for longer, a borrowing strategy that borrows long term funds as they are required may remain appropriate. Equally, variable rate funds (that avoid the cost of carry) or EIP (equal instalments of principal) that mitigate the impact are both active considerations.

4.8 The maximum maturity period for variable rate PWLB loans is ten years. Decisions to borrow at low, variable rates of interest will be taken after considering the absolute level of longer term interest rates, and their expected movement, together with the extent of variable rate earnings on the council's investment balances. When longer term rates move below the cost of variable rate borrowing any exposure to variable interest rates will be reviewed and, if appropriate, reduced.

4.9 The PWLB remains the preferred source of borrowing given the transparency and control that its facilities continue to provide.

4.10 The council has two bank loans of £6 million each which are LOBO loans (Lender's Option Borrower's Option). Each year, on the anniversary of taking out the loan, the lender may exercise their option to change the rate or terms of the loan. If this happens the council will consider the terms being offered and also repayment of the loan without penalty. The council may utilise cash resources for repayment or may consider replacing the loan.

4.11 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 continue to maintain a flexible policy for debt rescheduling. Current circumstances means opportunities for rescheduling debt will occur 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 the ratio of fixed to variable rate debt within the debt portfolio; or
- Amending the profile of maturing debt to reduce any inherent refinancing risks.

5.2 In September 2009, the PWLB issued a Consultation document, entitled 'PWLB Fixed Rates'. The result of this consultation process is still awaited but the likely outcome is a reduction in the extent of the margins between early repayment and new borrowing rates. This would make rescheduling less expensive and more attractive.

5.3 Any rescheduling activity will be undertaken within the council's treasury management policy and strategy. The council will agree in advance with their treasury advisers, 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).

6. INVESTMENT POLICY AND STRATEGY

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

6.2 To comply with the CLG's guidance, the council's general policy objective is to invest its surplus funds prudently. The council's investment priorities are:

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

The CLG's recent (draft) revised Guidance on investments reiterates security and liquidity as the primary objectives of a prudent investment policy. The speculative procedure of borrowing purely in order to invest is unlawful and the council will not engage in such activity.

6.3 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 Appendix 4.

6.4 The credit crisis has refocused attention on the treasury management priority of security of capital monies invested. The draft revisions to the CLG's Investment Guidance state that a specified investment is one made with a body or scheme of "high credit quality". The council will continue to maintain a counterparty list based on these criteria and will monitor and update the credit standing of the institutions on a regular basis. This assessment will include credit ratings and other alternative assessments of credit strength as outlined in paragraph 6.14. The CLG's Draft revisions to its Guidance on local government investments recommend that the Investment Strategy should set out the procedures for determining the maximum periods for which funds may prudently be committed. Such decisions will be based on an assessment of the authority's Balance Sheet position with the limit being set in Prudential Indicator 12 - Upper Limit for total principal sums invested over 364 days.

6.5 With regard to the council's Joint Ownership of West Mercia Supplies and the level of balances held by this organisation; the council may, if deemed in the best interest of prudent management of the West Mercia business undertake foreign currencies transactions, such as foreign exchange deals and investments. Such dealings must have relevance to the course of business of West Mercia Supplies. These dealings will be classified as non-specified as they are not sterling denominated.

6.6 The council's current level of investments is presented at Appendix 1.

Investment Strategy

6.7 The global financial situation in 2008 and 2009 has forced investors of public money to look carefully at the balance between risk and return.

6.8 The UK Bank Rate has been maintained at 0.5% since March 2009. Short-term money market rates are likely to remain at very low levels which will have a significant impact on investment income.

6.9 In any period of significant stress in the markets, the default position is for investments to be made with the government's Debt Management Office. This is viewed as the safest haven for council funds although the interest rate received is low (currently 0.25%).

6.10 At present the council has restricted its investment activity to:

- The Debt Management Agency Deposit Facility (The rates of interest from the DMADF are below equivalent money market rates. However, the returns are an acceptable trade-off for the guarantee that the council's capital is secure)
- AAA-rated Money Market Funds with a Constant Net Asset Value (CNAV)
- Deposits with other local authorities
- Business reserve accounts and term deposits. These are currently restricted to UK institutions that are rated at least A+ long term, and have access to the UK Government's 2008 Credit Guarantee Scheme (CGS)

6.11 Conditions in the financial sector have begun to show signs of improvement, albeit with substantial intervention by government authorities. In order to diversify the investment counterparty list, the use of comparable non-UK banks will be discussed with the council's treasury advisers as a possible option in 2010-11. Any decision will be made by the Director of Resources after seeking advice from our appointed advisors. The banks concerned are listed as potential counterparties in Appendix 4.

6.12 Counterparties are selected after analysis and careful monitoring of:

- Credit Ratings (minimum long-term AA-)
- Credit Default Swaps
- GDP; Net Debt as a Percentage of GDP
- Sovereign Support Mechanisms / potential support from a well-resourced parent institution
- Share Price

The council has also taken into account information on corporate developments and the view of the market sentiment. The council and its treasury advisors 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.

We remain sensitive to risk issues. Vigilance is key. However, recently the modest expansion of the counterparty list represents an incremental step to a return to a more active management. In order to meet requirements of the revised CIPFA Treasury Management Code, the council is focusing on a range of indicators (as stated above), not just credit ratings.

Limits for Specified Investments are set out in Appendix 4.

6.13 To protect against a prolonged period of low interest rates, one-year deposits and longer-term secure investments may be considered within the limits the council has set for Non-Specified Investments (see Appendix 4). Any non-specified investments would only be used after taking advice from the council's treasury adviser.

7. BALANCED BUDGET REQUIREMENT

7.1 It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the council to produce a balanced budget. A local authority is required to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from: -

- increases in interest charges caused by increased borrowing to finance additional capital expenditure; and
- any increases in running costs from new capital projects are limited to a level which is affordable within the projected income of the council for the foreseeable future.

8. 2010/11 MRP STATEMENT

Background:

8.1 For many years local authorities were 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). In practice MRP represents the financing of capital expenditure from the Revenue Account that was initially funded by borrowing.

8.2 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 replaced the formula based method for calculating MRP which existed under previous regulations under the Local Government Act 2003. The new regulations required 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 (CLG) produced Statutory Guidance which local authorities are required to follow, setting out what constitutes a prudent provision.

8.3 The CLG 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.

8.4 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.

8.5 The move to International Financial Reporting Standards (IFRS) means that Private Finance Initiative (PFI) schemes and Operating Leases may be brought on Balance Sheet. Where this is the case, such items are classed in accounting terms as a form of borrowing. CLG has therefore proposed amending the Capital Finance Regulations to ensure that the impact on the Revenue account is neutral, with MRP for these items matching the principal repayment embedded within the PFI or lease agreement.

Options for making 'Prudent Provision'

8.6 There are four options for Prudent Provision set out in the guidance:

Option 1 - Regulatory
For debt which is supported by the Government through Revenue Support Grant (RSG), authorities may continue to use the formulae under the 2003 Regulations, as RSG debt support is calculated in that way. This includes applying an adjustment (the Item A adjustment), which reduces the charge back to the former credit ceiling accounting methodology.

Option 2 - CFR method
This is similar to option 1, but just uses the CFR and doesn't apply the full formula, including the Item A adjustment. Under this option the annual repayment would be higher.

Option 3 - Asset Life Method
For new borrowing under the prudential system there are 2 options in the guidance. The first is to make provision over the estimated life of the asset for which the borrowing is undertaken. This can either be on an equal instalment method or an annuity basis.

Option 4 - Depreciation method
An alternative to Option 3 is to make provision in line with depreciation accounting. Although this would follow standard rules for depreciation accounting there would have to be some exceptions, for example, that MRP would continue until the provision is equal to the original debt and then cease.

MRP Policy 2010-11

8.7 In line with the guidance produced by the Secretary of State, the proposed policy for the 2010-11 calculation of MRP is as follows:

- Borrowing supported through the RSG grant system will be repaid in accordance with the 2003 Regulations.
- Prudential borrowing will be repaid over the life of the asset on an equal instalment basis commencing in the year following the year in which the asset first becomes operational.
- For expenditure under Regulation 25(1) (b), loans and grants towards capital expenditure by third parties, prudential borrowing will be repaid over the life of the asset in relation to which the third party expenditure is incurred.
- MRP in respect of PFI and leases brought on Balance Sheet, under the Code of Practice on Local Authority Accounting in the United Kingdom 2009 and IFRS, will match the annual principal repayment for the associated deferred liability.

9. REPORTING ON THE TREASURY OUTTURN

The Director of Resources will report to Cabinet, who oversee the scrutiny of treasury management activity / performance, as follows:

(a) A quarterly report will be produced monitoring performance against the strategy approved for the year. This will form part of the Council's overall monitoring reports.

(b) An outturn report for the year will be issued no later than 30th September after the financial year end.

APPENDIX 1

EXISTING PORTFOLIO PROJECTED FORWARD

	Current Portfolio £m	%	31 Mar 10 Estimate £m	31 Mar 11 Estimate £m	31 Mar 12 Estimate £m	31 Mar 13 Estimate £m
External Borrowing:						
Fixed Rate – PWLB	103		113	135	153	157
Fixed Rate – Market	12		12	12	12	12
Variable Rate – PWLB						
Variable Rate – Market						
Existing long-term liabilities	115		125	147	165	169
Investments:						
Managed in-house						
- Deposits and monies on call and Money Market Funds	26		10	5	16	16
(Net Borrowing Position)/ Net Investment position	89		115	142	149	153

Please note that the council is awaiting information relating to the inclusion of PFI-related deferred liabilities to the table above, and so the above figures are incomplete at this draft stage.

This outstanding information also affects many of the prudential indicators in Appendix B.

APPENDIX 2

PRUDENTIAL INDICATORS 2010/11 TO 2012/13

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, and issued a revised Code in November 2009.

2. Net Borrowing and the Capital Financing Requirement:

This is a key indicator of prudence. In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that the net external borrowing does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

The Director of Resources reports that the authority had no difficulty meeting this requirement in 2009/10, nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3. Estimates of Capital Expenditure:

3.1 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.

No. 1	Capital Expenditure	2009/10 Approved £'000	2009/10 Revised £'000	2010/11 £'000	2011/12 £'000	2012/13 £'000
	Total	**66,966**	**84,595**	**77,904**	**23,675**	**13,000**

3.2 Capital expenditure will be financed as follows:

Capital Financing	2009/10 Approved £'000	2009/10 Revised £'000	2010/11 £'000	2011/12 £'000	2012/13 £'000
Capital receipts	2,768	10,327	5,820	500	0
Grants and contributions	34,154	45,601	40,373	7,372	0
Supported borrowing	13,567	13,567	13,210	13,000	13,000
Unsupported borrowing	16,477	15,100	18,501	2,803	0
Total	**66,966**	**84,595**	**77,904**	**11,875**	**0**

Note: the element to be financed from borrowing impacts on the movement in the Capital Financing Requirement.

4. Ratio of Financing Costs to Net Revenue Stream:

4.1 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 in paragraph 68 of the Prudential Code.

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

No. 2	Ratio of Financing Costs to Net Revenue Stream	2009/10 Approved £'000	2009/10 Revised £'000	2010/11 £'000	2011/12 £'000	2012/13 £'000
	Net Revenue Stream	137,718	137,718	**143,143**	144,000	144,000
	Financing costs	13,176	12,401	**14,147**	15,226	15,577
	Percentage	**9.57%**	**9.00%**	**9.88%**	**10.57%**	**10.82%**

5. Capital Financing Requirement:

5.1 Capital expenditure may be financed by various means such as applying capital receipts, by a direct charge to revenue or by applying a capital grant. If it is not to be financed by such means, the capital expenditure will add to the capital financing requirement (CFR) of the council. Basically the CFR reflects the council's underlying need to borrow.

No. 3	Capital Financing Requirement	2009/10 Approved £'000	2009/10 Revised £'000	2010/11 £'000	2011/12 £'000	2012/13 £'000
	Total CFR	**180,697**	**173,170**	**193,639**	**199,125**	**202,228**

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

Capital Financing Requirement	2009/10 Approved £'000	2009/10 Revised £'000	2010/11 £'000	2011/12 £'000	2012/13 £'000
Balance B/F	158,249	150,375	171,450	193,639	199,125
Capital expenditure financed from borrowing (per 3.2)	30,044	28,430	31,711	15,803	13,559
Revenue provision for debt Redemption.	-7596	-7355	-9178	-10,317	-10,456
Balance C/F	**180,697**	**171,450**	**193,983**	**199,125**	**202,228**

Please note that the council is awaiting information relating to the inclusion of PFI-related deferred liabilities to the table above, and so the above figures are incomplete at this stage.

6. Actual External Debt:

6.1 This indicator is obtained directly from the council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities. This Indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

No. 4	Actual External Debt as at 31/03/2009	£'000
	Borrowing	120,870
	Other Long-term Liabilities	0
	Total	**120,870**

7. Incremental Impact of Capital Investment Decisions:

7.1 This is an indicator of affordability that shows the impact of capital investment decisions on council tax 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 Approved £	2010/11 £	2011/12 £	2012/13 £
	Increase in Band D Council Tax	23.68	**18.85**	11.71	2.16

8. Authorised Limit and Operational Boundary for External Debt:

8.1 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.

8.2 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.

8.3 The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements.

8.4 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 Approved £'000	2009/10 Revised £'000	2010/11 £'000	2011/12 £'000	2012/13 £'000
	Borrowing	190,000	150,000	**180,000**	205,000	225,000
	Other Long-term Liabilities	10,000	10,000	**10,000**	10,000	10,000
	Total	**200,000**	**160,000**	**190,000**	**215,000**	**235,000**

8.5 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.

8.6 The Director of Resources 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.

No. 7	Operational Boundary for External Debt	2009/10 Approved £'000	2009/10 Revised £'000	2010/11 £'000	2011/12 £'000	2012/13 £'000
	Borrowing	174,000	140,000	**165,000**	190,000	210,000
	Other Long-term Liabilities	6,000	6,000	**6,000**	6,000	6,000
	Total	**180,000**	**146,000**	**171,000**	**196,000**	**216,000**

9. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure:

9.1 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 net principal outstanding sums, (i.e. fixed rate debt net of fixed rate investments.

9.2 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 Approved %	2009/10 Revised %	2010/11 %	2011/12 %	2012/13 %
No. 9	**Upper Limit for Fixed Interest Rate Exposure**	100%	100%	100%	100%	100%
No. 10	**Upper Limit for Variable Interest Rate Exposure**	50%	50%	50%	50%	50%

9.3 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.

10. Maturity Structure of Fixed Rate borrowing:

10.1 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.

10.2 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.

<table>
<tr><th>No. 10</th><th>Maturity structure of fixed rate borrowing</th><th>Lower Limit %</th><th>Upper Limit %</th></tr>
<tr><td></td><td>under 12 months</td><td>0%</td><td>20%</td></tr>
<tr><td></td><td>12 months and within 24 months</td><td>0%</td><td>20%</td></tr>
<tr><td></td><td>24 months and within 5 years</td><td>0%</td><td>30%</td></tr>
<tr><td></td><td>5 years and within 10 years</td><td>0%</td><td>40%</td></tr>
<tr><td></td><td>10 years and within 20 years</td><td>0%</td><td>40%</td></tr>
<tr><td></td><td>20 years and within 30 years</td><td rowspan="4">50%</td><td>50%</td></tr>
<tr><td></td><td>30 years and within 40 years</td><td>100%</td></tr>
<tr><td></td><td>40 years and within 50 years</td><td>100%</td></tr>
<tr><td></td><td>50 years and above</td><td>100%</td></tr>
</table>

11. Upper Limit for total principal sums invested over 364 days:

11.1 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.

No. 11	Upper Limit for total principal sums invested over 364 days	2009/10 Approved £'000	2009/10 Revised £'000	2010/11 £'000	2011/12 £'000	2012/13 £'000
		10,000	10,000	10,000	10,000	10,000

Arlingclose's Economic and Interest Rate Forecast

The following is our advisors' report on economic and interest rate forecasts.

	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12
Official Bank Rate										
Upside risk				+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	0.50	0.50	0.50	0.50	1.00	1.50	2.25	3.00	4.00	4.00
Downside risk					-0.50	-0.50	-0.50	-0.25	-0.25	-0.25
1-yr LIBID										
Upside risk				+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	1.25	1.25	1.25	1.50	2.00	2.75	3.50	4.00	4.25	4.25
Downside risk					-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
5-yr gilt										
Upside risk		+0.25	+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	2.60	2.70	2.80	2.90	3.00	3.25	3.50	3.75	4.00	4.25
Downside risk		-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	+0.25	+0.25	+0.25
Central case	3.60	3.75	3.75	4.00	4.00	4.25	4.25	4.50	4.50	4.75
Downside risk			-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	+0.25	+0.25	+0.25
Central case	4.10	4.25	4.50	4.75	4.75	5.00	5.00	5.00	5.00	5.00
Downside risk		-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	+0.25	+0.25	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50	+0.50
Central case	4.00	4.25	4.50	4.50	4.50	4.75	4.75	4.75	4.75	4.75
Downside risk			-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, more "W" than "V" shaped. The Bank of England will stick to its lower-for-longer stance on policy rates.
- Gilt yields will remain volatile; yields have been compressed by Quantitative Easing and will rise once QE tapers off and if government debt remains at record high levels.
- Central banks will eventually wind down and exit their emergency liquidity provisions and shrink their balance sheets, but official interest rates in the UK, Eurozone and US will stay low for some while.
- There are significant threats to the forecast from potential downgrades to sovereign ratings and/or political instability.

APPENDIX 4

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 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).

"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
- AAA-rated Money Market Funds with a Constant Net Asset Value (Constant NAV)
- 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.

. * Investments in these instruments will be on advice from the council's treasury advisor.

For credit rated counterparties, the minimum criteria will be the short-term / long-term ratings assigned by Moody's Investors Services, Standard & Poor's or Fitch Ratings, as follows:

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

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**	**Counterparty**	**Maximum Limit of Investments £m**
Term Deposits	UK	DMADF, DMO	No limit
Term Deposits/ Call Accounts	UK	Other UK Local Authorities	No limit
Term Deposits/ Call Accounts	UK	Abbey	£5 million
Term Deposits/ Call Accounts	UK	Bank of Scotland/Lloyds	£5 million

Term Deposits/ Call Accounts	UK	Barclays	£5 million
Term Deposits/ Call Accounts	UK	Clydesdale	£5 million
Term Deposits/ Call Accounts	UK	HSBC	£5 million
Term Deposits/ Call Accounts	UK	Nationwide	£5 million
Term Deposits/ Call Accounts	UK	Royal Bank of Scotland	£5 million
Term Deposits/ Call Accounts	Australia	Australia and NZ Banking Group	£5 million
Term Deposits/ Call Accounts	Australia	Commonwealth Bank of Australia	£5 million
Term Deposits/ Call Accounts	Australia	National Australia Bank Ltd	£5 million
Term Deposits/ Call Accounts	Australia	Westpac Banking Corp	£5 million
Term Deposits/ Call Accounts	Canada	Bank of Montreal	£5 million
Term Deposits/ Call Accounts	Canada	Bank of Nova Scotia	£5 million
Term Deposits/ Call Accounts	Canada	Canadian Imperial Bank of Commerce	£5 million
Term Deposits/ Call Accounts	Canada	Royal Bank of Canada	£5 million
Term Deposits/ Call Accounts	Canada	Toronto-Dominion Bank	£5 million
Term Deposits/ Call Accounts	Finland	Nordea Bank Finland	£5 million
Term Deposits/ Call Accounts	France	BNP Paribas	£5 million
Term Deposits/ Call Accounts	France	Calyon (Credit Agricole Group)	£5 million
Term Deposits/ Call Accounts	France	Credit Agricole SA	£5 million
Term Deposits/ Call Accounts	Germany	Deutsche Bank AG	£5 million
Term Deposits/ Call Accounts	Netherlands	Rabobank	£5 million
Term Deposits/ Call Accounts	Spain	Banco Bilbao Vizcaya Argentaria	£5 million
Term Deposits/ Call Accounts	Spain	Banco Santander SA	£5 million
Term Deposits/ Call Accounts	Switzerland	Credit Suisse	£5 million
Term Deposits/ Call Accounts	US	JP Morgan	£5 million
Gilts	UK	DMO	No limit
Bonds	EU	European Investment Bank/Council of Europe	£5 million

AAA rated Money Market Funds	UK/Ireland/Luxembourg	CNAV MMFs	£5 million per fund
Other MMFs and CIS	UK	Collective Investment Schemes	£5 million

NB

Non-UK Banks - these will be restricted to a maximum exposure of 25% per country to limit the risk of over-exposure to any one country.
(Non-UK banks are not currently being used but, on the advice of the council's treasury advisor, Arlingclose Ltd, they may be considered in 2010-11)

MMFs – Arlingclose Ltd emphasise diversification for all investments including MMFs and advise that, as far as is practicable, the council should spread their investments in Money Market Funds between two funds or more.

Group Limits - For institutions within a banking group, Arlingclose advise a group 20% limit.

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:

	In-house use	Maximum maturity	Max % of portfolio	Capital expenditure?
▪ Deposits with banks and building societies ▪ Certificates of deposit with banks and building societies	✓ ✓	5 yrs	25% in aggregate	No
Gilts and bonds ▪ Gilts ▪ Bonds issued by multilateral development banks ▪ Bonds issued by financial institutions guaranteed by the UK government, e.g. GEFCO ▪ Sterling denominated bonds by non-UK sovereign governments	✓ (on advice from treasury advisor)	10 years	20% in aggregate	No
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) but which are not credit rated	✓ (on advice from treasury advisor)	These funds do not have a defined maturity date	20%	No
Government guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies (e.g. govt bonds issued by HBOS / RBS / Nationwide, etc)	✓	10 years	20%	Yes

Non-guaranteed bonds and debt instruments (e.g. floating rate notes) issued by corporate bodies	✓	10 years	20%	Yes
Collective Investment Schemes (Pooled funds) which do not meet the definition of collective investment schemes in SI 2004 No 534 or SI 2007 No 573	✓ (on advice from treasury advisor)	These funds do not have a defined maturity date	£20%	Yes

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.

For investing in banks for periods in excess of one year, the banks must have the following minimum credit ratings:

	Long-term	Short-term
Fitch	AA- (AA minus)	F1+
Moody's	Aa3	P-1
S&P	AA- (AA minus)	A-1+