Report to: **Cabinet**

Subject: **Integrated Treasury Management Strategy Statement 2012/13, Annual Investment Strategy 2012/13 and Minimum Revenue Provision Policy Statement 2012/13**

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1. PURPOSE OF REPORT

To present for Members' approval, the Council's integrated Treasury Management Strategy Statement (TMSS), Annual Investment Strategy (AIS), and Minimum Revenue Provision Policy (MRPP) for 2012/13.

2. BACKGROUND

2.1 Definition

Treasury management is defined as "the management of the local authority'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. "

It is a statutory requirement for the Council to produce a "balanced budget", which broadly means that cash raised during the year will meet cash expenditure. Sections 72 to 79 of the 2011 Localism Act places a duty on a local authority to calculate its "council tax requirement" for each financial year, and this includes the revenue costs which result from the capital investment decisions of the authority.

Part of the treasury management service is to ensure that cashflow is adequately planned, with cash being available when it is needed. Surplus cash is invested with counterparties commensurate with the Council's low risk appetite.

A further treasury management function is the funding of capital plans. The capital plans provide a guide to the Council's borrowing needs and require longer term cashflow planning to ensure the Council can meet its spending obligations. The management of longer term cash may involve arranging long or short term loans or the use of longer term cashflow surpluses.

2.2 Statutory Reporting Requirements

The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised November 2009) was adopted by the Council on 3 March 2010. The Code requires the creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities, and Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

In addition, the Council is required to approve a minimum of three treasury management reports annually, incorporating a range of policies, estimates and actuals. Scrutiny of treasury management strategy and policies must be delegated to a specific named body, therefore all treasury management reports are initially considered by Cabinet, before being recommended to Council. Delegation arrangements further require that reports are reviewed by the Scrutiny Committee.

a. Treasury Management Strategy Statement (TMSS) incorporating the Prudential and Treasury Indicators (see below)

This is the most important report and covers:

- capital plans, including Prudential indicators - the Local Government Act 2003 (the Act) and supporting regulations requires the Council to "have regard to" the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

- the Minimum Revenue Provision (MRP) Policy, which sets out how residual capital expenditure is to be charged to revenue over time.

- the Treasury Management Strategy, which sets out how borrowings and investments are to be organised.

- the investment strategy, which specifies the parameters on how investments are to be managed. Priority is given to the security and liquidity of investments which are undertaken in accordance with revised investment guidance issued by the Department of Communities and Local Government (CLG) in April 2010.

b. Mid-year Treasury Management Report

This report is required to update members with the progress of the capital position, and to amend Prudential and Treasury Indicators where appropriate.

Gedling Borough Council has long adopted a policy of presenting quarterly treasury management reports to Cabinet, and this exceeds the minimum requirement.

c. Annual Treasury Report

This "stewardship" report provides details of a selection of actual prudential and treasury indicators, and actual treasury operations, compared to the estimates within the strategy.

3. TREASURY MANAGEMENT STRATEGY STATEMENT (TMSS) FOR 2012/13

3.1 Introduction

The TMSS covers two main areas:

- Capital issues
    - the Capital Plans and the Prudential Indicators (3.2)
    - the MRP strategy (3.3)
- Treasury Management issues
    - the current treasury position (3.4)
    - treasury indicators limiting treasury risk (3.5)
    - prospects for interest rates (3.6)
    - borrowing strategy (3.7)
    - policy on borrowing in advance of need (3.8)
    - debt rescheduling (3.9)
    - Annual Investment Strategy (AIS) including policies on creditworthiness and external service providers(AIS) (3.10)

The elements within these areas cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, The CLG MRP Guidance, the CIPFA Treasury Management Code, and the CLG Investment Guidance.

3.2 The Capital Prudential Indicators 2012/13 to 2014/15

At the meeting on 12 January 2012 Cabinet considered a set of Prudential Indicators and referred them for approval by Full Council on 22 February 2012. Since that meeting some minor amendments have been made to the proposed capital programme including the schemes approved by Cabinet for deferral from the 2011/12 budget as part of the normal quarterly monitoring processes. The 2012/13 Capital Programme report, an item elsewhere on this agenda, provides full details of the proposed programme. As a result some minor amendments are required to the Prudential Indicators and the revised figures are included at Appendix 1. The revised indicators represent capital investment plans that are affordable, prudent and sustainable which have been fully factored into the Council's Medium Term Financial Plan.

a. Capital Expenditure

The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the Prudential Indicators, which are designed to assist members with their overview and confirmation of those capital expenditure plans. The indicator includes a summary of both the capital expenditure plans previously agreed, and those that are part of the current cycle.

b. Capital Financing Requirement (CFR)(the Council's borrowing need)

The CFR represents the total historic capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure not immediately financed, for example by capital receipts, will increase the CFR. Following accounting changes, the CFR now includes PFI schemes and finance leases which have been brought onto the balance sheet, however the Council does not currently hold any of these items.

c. Ratio of financing costs to net revenue stream

This indicator identifies the trend in the cost of capital (borrowing and other long-term obligation costs, net of investment income) against the net revenue stream of the Council. Estimates of financing costs include current commitments, and the effects of the proposals within the current cycle.

d. Incremental impact of 2012/13 capital investment decisions on council tax

This indicator identifies the revenue costs associated with proposed changes to the capital programme, recommended in the current cycle, compared to the existing approved commitments and current plans.

3.3 Minimum Revenue Provision (MRP) Policy Statement

Capital expenditure is that on assets with a life expectancy of more than one year, for example, buildings, vehicles, machinery etc. Each year, the Council is required to pay off part of its accumulated capital expenditure by way of a revenue charge, ie. a "minimum revenue provision" (MRP).

CLG regulations require the Council to approve an MRP Statement in advance of each financial year. The Council must determine an amount of MRP that it considers to be "prudent", the broad aim being to ensure that borrowing is repaid over a period that reflects the useful lives of the assets acquired. The Council is obliged to have regard to the CLG guidance, but it is not prescriptive. The guidance does not, however, define "prudent", instead making recommendations on the interpretation of the term. It is the responsibility of each authority to decide upon the most appropriate method of making a prudent MRP, having had regard to the guidance and its own circumstances. The following options are provided:

- Option 1 the Regulatory Method - MRP is equal to the amount determined under the former regulations of the 2003 Act, as if they had not been revoked by the 2008 Act. This method must continue for all capital expenditure incurred in years before the start of the new MRP arrangements. It may also be used for new Government-supported borrowing supported under the grant system, but not for new prudential (self-financed) borrowing.

- Option 2 the Capital Financing Requirement Method - this method is based on 4% of the Capital Financing Requirement (CFR). The CFR is a measure of the authority's outstanding debt liability and is balance sheet derived. The method may also be used for new borrowing supported under the grant system, but not for new prudential borrowing.

- Option 3 the Asset Life Method - this method may be applied to new capital expenditure financed by both Government-supported borrowing and prudential borrowing. It is intended that MRP should be spread over the useful lives of the assets created. Advantages of this method are that borrowing for longer life assets, eg. freehold land, can be spread over much longer periods than would arise under Options 1 or 2, and that no MRP is made until the financial year in which expenditure on the asset is fully incurred or, in the case of a new asset, it comes into service. This "MRP holiday" is not available under Options 1 or 2.

  Option 3 should be applied where an authority incurs expenditure which is financed by borrowing, and is treated as capital expenditure by virtue of a direction under section (2)(b) of the 2003 Act, or regulation 25(1) of the 2003 regulations, eg, grants towards capital expenditure by third parties. The MRP guidance indicates the number of years of "useful life" to be used for each type of expenditure in this category.

  MRP under Option 3 may be calculated using either an equal instalment method, or an annuity method, whereby annual payments gradually increase during the life of the asset.

- Option 4 the Depreciation Method - this method may be applied to new capital expenditure financed by both Government-supported borrowing and prudential borrowing. MRP charges are linked to the useful life of each type of asset using the standard accounting rules for depreciation, but with some exceptions, ie. it is a more complex approach than Option 3.

The following MRP Policy Statement is proposed for 2012/13:

a. The Council will assess MRP in accordance with the recommendations within the guidance issued under section 21(1A) of the Local Government Act 2003

b. Option 1, the regulatory method, will be used for calculating MRP in respect of all capital expenditure incurred up to and including 31 March 2008.

c. Option 3, the Asset Life Method, will be used for calculating MRP in respect of all capital expenditure incurred on and after 1 April 2008. An equal instalment approach will be adopted.

d. The CFO will determine estimated asset lives. Where expenditure of different types is involved, it will be grouped together in a manner which best reflects the nature of the main component of expenditure. It will only be divided up in cases where there are two or more major components, with significantly different asset lives.

e. When the Council undertakes self-financed borrowing under the Prudential Code to acquire an asset and makes MRP based on the asset life method, there is still a rise in CFR, which is in turn the basis of the MRP calculation under the old regulatory method, potentially leading to a double count. Accordingly the new arrangements provide for the use of an ”adjusted version of the CFR”, solely for the purpose of calculating MRP on expenditure falling under the old regulatory method (see option 1 above).

f. The Council intends to operate the Local Authority Mortgage Scheme from 1 April 2012, using a cash-backed option. The mortgage lender requires a five-year deposit to match the five-year life of the indemnity. The deposit placed with the mortgage lender provides an integral part of the mortgage lending, and is treated as capital expenditure, and a loan to a third party, therefore the Capital Financing Requirement (CFR) will increase by the amount of the total indemnity. The deposit is due to be returned in full at maturity, with interest paid either annually or on maturity. Once the funds are returned to the Council, they will be classed as a capital receipt, and the CFR will reduce accordingly. As this is a temporary (5-year) arrangement, and the funds will be returned in full, there is no need to set aside prudent provision to repay the debt liability in the interim period, and there is accordingly no MRP application.

g. In view of the economic climate and significant budgetary pressures, the Council will not provide for an additional voluntary contribution to MRP in 2012/13.

   Based on the above policy, the total MRP charge for 2012/13 has been calculated as £512,500, as detailed below, and this sum has been included in the Council’s 2012/13 budget proposals. The exact amount of MRP will be subject to change should capital financing decisions alter during the year.

	£
Option 1 – Regulatory Method	303,500
Option 3 – Asset Life Method	209,000
Total MRP	**512,500**

3.4 The Council's current Treasury portfolio position

The Council must ensure that its total debt, net of any investments (ie. net debt) does not, except in the short term, exceed the total of the CFR in the preceding year (the opening CFR), plus the estimates of any additional CFR for the coming year and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Council's actual treasury portfolio position at 31 March 2011, together with forward projections, is summarised below. The table shows the expected actual external debt against the underlying capital borrowing need (the CFR).

	2010/11 Actual	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
	£000s	£000s	£000s	£000s	£000s
External Debt:					
Debt at 1 April	9,812	9,812	9,812	11,012	12,805
Change in debt in yr	0	0	1,200	1,793	1,299
Debt at 31 March	**9,812**	**9,812**	**11,012**	**12,805**	**14,104**
Investments	-7,010	-5,500	-5,000	-4,000	-3,500
Net Debt	**2,802**	**4,312**	**6,012**	**8,805**	**10,604**
Opening CFR	9,283	9,779	10,732	13,095	13,696
Mvt in yr + next 2 yrs	2,909	3,684	3,475	658	904
Maximum	**12,192**	**13,463**	**14,207**	**14,563**	**14,600**
Over/(Under) Borrwg	**(9,390)**	**(9,151)**	**(8,195)**	**(5,758)**	**(3,996)**

The CFO reports that the Council has complied with this prudential indicator during the current year, and does not envisage any difficulties for the future. This view takes into account current commitments and the proposals in the current cycle.

3.5 Treasury indicators – Limits to Borrowing Activity

a. Operational Boundary

This represents a limit beyond which external debt is not expected to go, given "normal" operations, and is a key tool for in-year monitoring. It is set to reflect the CFO's prudent, but not worst case, scenario, and is based on the opening CFR for the relevant year, plus the expected movements for the year, and the following two years, plus an allowance for cashflow borrowing. It is split between borrowing and other long-term liabilities, but the CFO has delegated authority to effect movement between the separately agreed figures.

b. Authorised Limit

This represents a control on the maximum level of borrowing and reflects a level of debt which whilst not desirable, is affordable in the short term. It is not sustainable in the long term.

The authorised limit for external debt represents the statutory limit under section (1) of the Local Government Act 2003.

3.6 Prospects for Interest Rates

The Council has appointed Sector as its treasury advisors, and part of their service is to assist the Council to formulate a view on interest rates. Appendix 2 draws together a number of current City forecasts for short term (Bank Rate) and longer fixed interest rates. The following table gives a summary of the Sector central view:

Annual Average %	Bank Rate	Money Rates		PWLB Borrowing Rates		
		3 month	1 year	5 year	25 year	50 year
March 2012	0.50	0.70	1.50	2.30	4.20	4.30
June 2012	0.50	0.70	1.50	2.30	4.20	4.30
Sept 2012	0.50	0.70	1.50	2.30	4.30	4.40
Dec2012	0.50	0.70	1.60	2.40	4.30	4.40
March 2013	0.50	0.75	1.70	2.50	4.40	4.50
June 2013	0.50	0.80	1.80	2.60	4.50	4.60
Sept 2013	0.75	0.90	1.90	2.70	4.60	4.70
Dec 2013	1.00	1.20	2.20	2.80	4.70	4.80
March 2014	1.25	1.40	2.40	2.90	4.80	4.90
June 2014	1.50	1.60	2.60	3.10	4.90	5.00

Growth in the UK economy is expected to be weak in the next two years and there is a risk of a technical recession (i.e. two quarters of negative growth). Bank Rate, currently 0.5%, underpins investment returns and is not expected to start increasing until quarter 3 of 2013 despite inflation currently being well above the Monetary Policy Committee inflation target. Hopes for an export led recovery appear likely to be disappointed due to the Eurozone sovereign debt crisis depressing growth in the UK's biggest export market. The Comprehensive Spending Review, which seeks to reduce the UK's annual fiscal deficit, will also depress growth during the next few years.

Fixed interest borrowing rates are based on UK gilt yields. The outlook for borrowing rates is currently much more difficult to predict. The UK total national debt is forecast to continue rising until 2015/16, and the consequent increase in gilt issuance is therefore expected to be reflected in an increase in gilt yields over this period. However, gilt yields are currently at historically low levels due to investor concerns over Eurozone sovereign debt and have been subject to exceptionally high levels of volatility as events in the Eurozone debt crisis have evolved.

This challenging and uncertain economic outlook has a several key treasury mangement implications:

- The Eurozone sovereign debt difficulties, most evident in Greece, provide a clear indication of much higher counterparty risk. This continues to suggest the use of higher quality counterparties for shorter time periods;
- Investment returns are likely to remain relatively low during 2012/13;
- Borrowing interest rates are currently attractive, but may remain low for some time. The timing of any borrowing will need to be monitored carefully;
- There will remain a cost of capital – any borrowing undertaken that results in an increase in investments will incur a revenue loss between borrowing costs and investment returns.

3.7 Borrowing Strategy

a. The Strategy

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the CFR), has not been fully funded with loan debt, as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is high.

Against this background and the risks within the economic forecast, caution will be adopted with the 2012/13 treasury operations. The CFO will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates,* e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

- *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast,* perhaps arising

from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.
Any decisions will be reported to Cabinet at the next available opportunity.

Any new borrowing will be discussed with Sector. The following options may be considered:

- The cheapest borrowing will be internal borrowing, ie. running down of cash balances and forfeit of small amounts of interest, earned at historically low rates. In view of the overall forecast for long-term borrowing rates to rise over the next few years, consideration will also be given to weighing the short term advantage of such internal borrowing against potential long term costs, ie. if the opportunity is missed for taking loans at long-term rates which will be even higher in future.
- Temporary borrowing from the market, or from other local authorities.
- PWLB variable rate loans for up to 10 years.
- Long-term fixed rate market loans at rates significantly below PWLB rates for the equivalent maturity period (where available), and to maintaining an appropriate balance between PWLB and market debt in the debt portfolio.
- PWLB borrowing for periods under 10 years where rates are expected to be significantly lower than rates for longer periods. This offers a range of options for new borrowing which will spread debt maturities away from a concentration in longer dated debt.
- PWLB borrowing by annuity and EIP loans, as well as maturity loans.

b. Treasury Management Limits on Activity

Three debt related treasury activity limits are set with the purpose of restraining the treasury function within certain boundaries and hence managing risk and reducing the impact of any adverse movements in interest rates. However, care must be taken when setting these limits since if they are set to be too restrictive, they may impair opportunities to reduce cost or improve performance. The indicators are:

- Upper limits on variable interest rate exposure - this identifies a maximum limit for variable interest rates based upon the debt position net of investments

- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates. Additional local indicators are also shown purely for either debt or investments.

- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

3.8 Policy on borrowing in advance of need

The Council will not borrow more than, or in advance of, its needs purely to profit from the investment of the extra sums borrowed, since this is illegal. Any decision to borrow in advance of need will within the forward-approved CFR estimates, and will be considered carefully to ensure value for money can be demonstrated, and that the Council can ensure the security of such funds.

In determining whether borrowing will be undertaken in advance of need, the Council will ensure that there is a clear link between the capital programme and the maturity profile of the existing debt portfolio which supports the need to take funding in advance of need. It will ensure that the ongoing revenue liabilities created, and the implications for the future plans of and budgets have been considered, and evaluate the economic and market factors that might influence the manner and timing of any decision to borrow. The advantages and disadvantages of alternative forms of funding will be considered, together with the most appropriate periods over which to fund.

3.9 Debt Rescheduling

As short-term borrowing rates will be considerably cheaper than longer-term fixed interest rates, there may be potential for some residual opportunities to generate savings by switching from long-term to short-term debt, however, these savings will need to be considered in the light of the premiums incurred, their short nature, and the likely cost of refinancing them once they mature, compared to the current rates on longer term debt in the existing debt portfolio. Any such rescheduling is likely to cause a flattening of the Council's maturity profile, as in recent years there has been a skew towards longer dated PWLB.

The reasons for any rescheduling to take place will include:

- The generation of cash savings and/or discounted cashflow savings, at minimum risk
- Helping to fulfil the treasury strategy
- Enhancing the balance of the portfolio (amend the maturity profile and/or the balance of volatility)

All rescheduling will be reported to Cabinet at the meeting following its action.

3.10 Annual Investment Strategy 2012/13

The intention of the strategy is to provide security of investment and the minimisation of risk. The aim is to generate a list of highly creditworthy counterparties which will also enable divesification and thus avoidance of concentration risk.

a. Investment Policy

The Council's investment policy has regard to the CLG's guidance on Local Government Investments ("the guidance"), and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code").

All investments will be made in sterling, and the Council's general policy objective is the prudent investment of its treasury balances. The Council's investment priorities are firstly the security of capital, secondly the liquidity of its investments, and thirdly the rate of return. The risk appetite of the Council is low, in order to give priority to the security of its investments.

The borrowing of monies purely to invest or on-lend and make a return remains unlawful, and the Council will not engage in such activity.

In accordance with the above guidance from the CLG and CIPFA, and in order to minimise the risk to investments, the Council has below clearly stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list. The creditworthiness methodology uses the Sector ratings service whereby banks' ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications.

The Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "credit default swaps" and overlay that information on top of the credit ratings.

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

Investment instruments identified for use in the financial year are listed at Appendix 4 under "Specified" and "Non-Specified" categories. An investment is a specified investment if all of the following apply:

- The investment is denominated in sterling and the payment or repayment is only payable in sterling.
- The investment is not a long-term investment, ie. less than one year.
- The making of the investment is not defined as capital expenditure.
- The investment is made with a body of high credit quality, or with the UK government, a local authority or a parish council.

Only minimal reference need be given to specified investments in the Annual Investment Strategy, and they will generally be used for cash-flow management.

Non-specified investments are all those not meeting the criteria for specified investments. They may on occasion be made with the same counterparty as specified investments, being non-specified only by way of the maturity period being over one year. Alternatively they may be more complex instruments, or those offering slightly higher risk or lower liquidity. If used at all, non specified investments will tend only to be used for the longer-term investment of core-balances.

Appendix 4 also sets out:

- The advantages and associated risk of investments under the non-specified category
- The upper limit to be invested in each non-specified category
- Which instruments would best be used after consultation with the Council's treasury advisers.
  Counterparty limits will be as set out in the Council's Treasury Management Practices (Schedules).

b. Creditworthiness Policy

The primary principles governing the Council's investment criteria are:

- Security of capital
- Liquidity of capital
- Return on investment

With regard to security, policies are maintained for the "categories" of investment to be used, and these are set out in the Specified and Non-Specified investment sections at 3.10.1 above, and at Appendix 4. For the purpose of liquidity, policies are in place for determining the maximum periods for which funds may prudently be committed.

The CFO also maintains a "counterparty list" using rating information is provided by Sector, which is monitored constantly. The CFO has delegated authority to amend the minimum criteria as he sees fit, and will report any such amendments to Cabinet for information as necessary. For example, following notification of the downgrade by Fitch of most of the UK banking institutions on 13 October 2011, the council's minimum lending criteria became unworkable.

Furthermore, Sector's creditworthiness reports had indicated for some time that Fitch would review their "individual" strength ratings and move to a "viability" rating. The viability scheme splits the old A,B,C ratings down much further, allowing decisions to be made in finer detail. For example, to exactly match the former A to C categories, a change to AAA to BB+ would have been made. However, BB denotes "moderate" prospects for ongoing viability ie. a "moderate" degree of financial strength exists, which would have to be eroded before the bank would have to rely on external support. On the other hand, BBB denotes “good” fundamental credit quality. The opportunity to fine tune the acceptable level of risk was taken by the CFO and the currently approved minimum criteria are as follows:

Criterion	Minimum Rating
Long Term rating	A or better
Short Term rating	F1 or better
Viability rating	AAA to BBB
Support (Govt etc)	1, 2 or 3

Country creditworthiness considerations – appendix 5 sets out the countries currently meeting the criteria for investment by the Council. However, for some time the CFO has adopted a policy to lend only to UK registered institutions, and this will continue for 2012/13. Given the extreme volatility of market conditions, this policy will of course be subject to ongoing review by the CFO, in conjunction with advice from Sector.

LAMS - Under the recently approved Local Authority Mortgage Scheme, the Council is required to place funds of £1m, with Lloyds Banking Group for a period of five years. This is classified as being a “service investment”, rather than a treasury management investment, and is therefore outside of the Specified/Non specified categories.

c. Investment Strategy

The Council’s in-house managed funds are mainly cash-flow derived, however, there has for some time been a core balance available for investment over a 2-3 year period if appropriate. In addition, borrowing undertaken in advance of need at favourable interest rates has recently added to the funds available.

Investments will be made with careful reference to any remaining core balance, to cash-flow requirements, and to the outlook for short-term interest rates (ie. for investments up to 12 months).

Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 3 of 2013. Bank Rate forecasts for financial year ends (March) are:

- 2011/ 2012 0.50%
- 2012/ 2013 0.50%
- 2013/ 2014 1.25%
- 2014/ 2015 2.50%

There are downside risks to these forecasts (ie. the start of increases in Bank Rate is delayed even further) if economic growth remains weaker for longer than expected. However, should the pace of growth pick up more sharply than expected there could be upside risk, particularly if the Bank of England inflation forecasts for two years ahead exceed the 2% target rate.

In view of the above forecasts for Base Rate, Sector's suggested target rates for new cash-flow generated balances placed for periods up to three months during each of the next five financial years are shown below. The Council will seek to use its corporate deposit accounts and short-dated fixed term deposits (1-3 months) in order to benefit from the compounding of interest.

- 2012/13 0.70%
- 2013/14 1.00%
- 2014/15 1.60%
- 2015/16 3.30%
- 2016/17 4.10%

Limits must be set for the total principal funds permitted for investment for periods in excess of 364 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end. The limit for new 2012/13 investments maturing beyond 31 March 2013 is £5m, beyond 31 March 2014 is £3m and beyond 31 March 2015 is £1m.

d. Investments defined as capital expenditure

The acquisition of share capital or loan capital in a body corporate is defined as capital expenditure under regulation 25(1)(d) of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. Such investments will have to be funded out of capital or revenue resources, and will be classified as non-specified investments. Investments in "money market funds", which are collective investment schemes, and bonds issued by "multilateral development banks", both defined in SI 2004 No 534, will not be treated as capital expenditure. A loan or grant or financial assistance by this Council to another body for capital expenditure by that body will be treated as capital expenditure.

e. Provision for credit-related loss

If any of the Council's investments appear to be at risk of loss due to default, ie this is a credit-related loss and not one resulting from a fall in price due to movements in interest rates, the Council will make revenue provision of an appropriate amount.

f. End of Year Investment Report

At the end of the year, the Council will report on its investment activity as part of its Annual Treasury Report.

g. Policy on the use of external service providers

The Council uses Sector as its external treasury management advisers, however it recognises that responsibility for treasury management decisions remains with the organisation at all times, and will ensure that undue reliance is not placed upon external service providers.

The Council also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

4. Scheme of Delegation

Full Council is responsible for:

- Receiving and reviewing reports on treasury management policies, practices and activities
- Approval of the annual strategy (TMSS)

Cabinet is responsible for:

- Approval of/amendments to the Council's adopted clauses, treasury management policy statement and treasury management practices
- Budget consideration and approval
- Approval of the division of responsibilities
- Receiving and reviewing regular Treasury Management monitoring reports, and acting on recommendations
- Approving the selection of external service providers and agreeing terms of appointment.

Audit Committee is responsible for:

- Reviewing the treasury management policy and procedures and making recommendations to the responsible body.

5. The role of the Section 151 Officer

The CFO is the nominated S151 Officer. The role of the S151 (responsible) officer includes the following:

- recommending clauses, treasury management policy/practices for approval, reviewing these regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function

- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers.

6. RECOMMENDATION

It is recommended that:

Members note the Integrated Treasury Management Strategy Statement 2012/13, (incorporating the Annual Investment Strategy and Minimum Revenue Policy Statement) and the revised Prudential Indicators at Appendix 1, as detailed in the report, and refer it to Full Council for approval as required by the regulations.

Appendix 1 Prudential and Treasury Indicators
Appendix 2 Interest rate forecasts
Appendix 3 Economic background
Appendix 4 Specified and non-specified investments
Appendix 5 Approved countries for Investment

APPENDIX 1

Prudential and Treasury Indicators for 2012/13 to 2014/15

Prudential Indicators

	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
a) Capital Expenditure	£3,958,200	£1,761,000	£1,808,000
b) Ratio of Financing Costs to Net Revenue Stream	6.46%	8.06%	9.35%
c) Capital Financing Requirement (CFR)	£13,095,100	£13,696,200	£14,207,400
d) Net Borrowing and CFR	£14,207,400	£14,563,200	£14,600,000
e) Incremental impact of new 2012/13 capital investment decisions	£0.57	£4.28	£4.26

Treasury Management Indicators

	2012/13 Estimate	2013/14 Estimate	2014/15 Estimate
a) Authorised Limit for External Debt:			
Borrowing	£16,200,000	£16,600,000	£16,600,000
Other Long Term Liabilities	£1,500,000	£1,500,000	£1,500,000
Total Authorised Limit	**£17,700,000**	**£18,100,000**	**£18,100,000**
b) Operational Boundary for External Debt:			
Borrowing	£15,200,000	£15,600,000	£15,600,000
Other Long Term Liabilities	£1,500,000	£1,500,000	£1,500,000
Total Operational Boundary	**£16,700,000**	**£17,100,000**	**£17,100,000**
c) Upper limit for fixed interest exposure (Max o/s net Borrowing)	£14,200,000	£14,600,000	£14,600,000
Local indicator-Investment only	100%	100%	100%
Local indicator-Borrowing only	100%	100%	100%
d) Upper limit for variable interest exposure (Max o/s net Borrowing)	£2,000,000	£2,000,000	£2,000,000
Local indicator-Investment only	100%	100%	100%
Local indicator-Borrowing only	50%	50%	50%
e) Upper limits for maturity structure of outstanding borrowing during 2012/13 (Lower limit 0% in all cases)			
Under 1 year	20%		
1-2 years	25%		
2-5 years	50%		
5-10 years	50%		
Over 10 years	100%		
f) Upper limits for principal sums invested for periods **over** 364 days			
Maturing beyond 31 March 2013	£5,000,000		
Maturing beyond 31 March 2014	£3,000,000		
Maturing beyond 31 March 2015	£1,000,000		

Sector's Interest Rate View															
	Now	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15
Sector's Bank Rate View	**0.50%**	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	2.00%	2.25%	2.50%
3 Month LIBID	**0.87%**	0.70%	0.70%	0.70%	0.70%	0.70%	0.75%	0.80%	0.90%	1.20%	1.40%	1.60%	2.10%	2.40%	2.60%
6 Month LIBID	**1.16%**	1.00%	1.00%	1.00%	1.00%	1.00%	1.10%	1.20%	1.40%	1.60%	1.80%	2.00%	2.50%	2.70%	2.90%
12 Month LIBID	**1.65%**	1.50%	1.50%	1.50%	1.50%	1.60%	1.70%	1.80%	1.90%	2.20%	2.40%	2.60%	3.10%	3.20%	3.30%
5yr PWLB Rate	**2.25%**	2.30%	2.30%	2.30%	2.30%	2.40%	2.50%	2.60%	2.70%	2.80%	2.90%	3.10%	3.30%	3.50%	3.70%
10yr PWLB Rate	**3.33%**	3.30%	3.30%	3.30%	3.40%	3.40%	3.50%	3.60%	3.70%	3.80%	4.00%	4.20%	4.40%	4.60%	4.80%
25yr PWLB Rate	**4.24%**	4.20%	4.20%	4.20%	4.30%	4.30%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%
50yr PWLB Rate	**4.26%**	4.30%	4.30%	4.30%	4.40%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%	5.30%
Bank Rate															
Sector's View	**0.50%**	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	2.00%	2.25%	2.50%
UBS	**0.50%**	0.50%	0.50%	0.50%	0.50%	0.50%	-	-	-	-	-	-	-	-	-
Capital Economics	**0.50%**	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	-	-	-	-	-
5yr PWLB Rate															
Sector's View	**2.25%**	2.30%	2.30%	2.30%	2.30%	2.40%	2.50%	2.60%	2.70%	2.80%	2.90%	3.10%	3.30%	3.50%	3.70%
UBS	**2.25%**	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Capital Economics	**2.25%**	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	-	-	-	-	-
10yr PWLB Rate															
Sector's View	**3.33%**	3.30%	3.30%	3.30%	3.40%	3.40%	3.50%	3.60%	3.70%	3.80%	4.00%	4.20%	4.40%	4.60%	4.80%
UBS	**3.33%**	3.45%	3.45%	3.50%	3.60%	3.65%	-	-	-	-	-	-	-	-	-
Capital Economics	**3.33%**	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	-	-	-	-	-
25yr PWLB Rate															
Sector's View	**4.24%**	4.20%	4.20%	4.20%	4.30%	4.30%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%
UBS	**4.24%**	4.80%	4.90%	4.90%	4.90%	4.90%	-	-	-	-	-	-	-	-	-
Capital Economics	**4.24%**	4.30%	4.30%	4.30%	4.30%	4.30%	4.30%	4.30%	4.30%	4.30%	-	-	-	-	-
50yr PWLB Rate															
Sector's View	**4.26%**	4.30%	4.30%	4.30%	4.40%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%	5.30%
UBS	**4.26%**	4.80%	4.95%	4.95%	5.00%	5.00%	-	-	-	-	-	-	-	-	-
Capital Economics	**4.26%**	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	-	-	-	-	-

APPENDIX 2

APPENDIX 3

ECONOMIC BACKGROUND

(a) The Global Economy

The outlook for the global economy remains clouded with uncertainty with the UK economy struggling to generate sustained recovery that offers solid optimistim for the outlook for 2012, or possibly even into 2013. Consumer and business confidence levels are low and with little to boost sentiment, it is not easy to see potential for a significant increase in the growth rate in the short term.

At the centre of much of the uncertainty is the ongoing Eurozone sovereign debt crisis which has intensified, rather than dissipated throughout 2011. The main problem has been Greece, where, even with an Eurozone/IMF/ECB bailout package and the imposition of austerity measures aimed at deficit reduction, the lack of progress and the ongoing deficiency in addressing the underlying lack of competitiveness of the Greek economy, has seen an escalation of their problems. These look certain to result in a default of some kind but it currently remains unresolved if this will be either “orderly” or “disorderly”. Most commentators currently view that it is now inevitable that Greece will have to exit the Eurozone in 2012.

There is also growing concern about the situation in Italy and the risk that contagion has not been contained. Italy is the third biggest debtor country in the world but its prospects are limited given the poor rate of economic growth over the last decade and likely difficulties in implementing the required level of fundamental reforms in the economy. The Eurozone now has a well established track record of always doing too little too late to deal with this crisis; this augurs poorly for future prospects, especially given the rising level of electoral opposition in northern EU countries to bailing out profligate southern countries.

The US economy has encouraged with some positive news around the start of 2012 but any improvement in the weak rate of growth is likely to only generate slow progress in reducing the high level of unemployment which is acting as such a dampener on the economy. With Presidential elections due in November 2012, the current administration has been hamstrung by political gridlock with the two houses split between the main parties. In quarter 3 the Federal Reserve started “Operation Twist” in an effort to re-ignite the rate of growth in the economy. However, high levels of consumer indebtedness, a moribund housing market together with stubbornly high unemployment, will continue to weigh heavily on consumer confidence and so on the abiltity to generate a healthy and consistent rate of economic growth.

Hopes for broad based recovery have, therefore, focussed on the emerging markets but these areas have been struggling with inflationary pressures in their previously fast growth economies. China, though, has maintained its growth pattern, despite a major thrust to tighten monetary policy during 2011 to cool inflationary pressures which are now subsiding. However, some forward looking indicators are causing concern that there may not be a soft landing ahead, which would then be a further dampener on world economic growth.

(b) The UK economy

The Government's austerity measures, aimed at getting the public sector deficit into order over the next four years, have yet to fully impact on the economy. However, coming at a time when economic growth has been weak and concerns at the risk of a technical recession (two quarters of negative growth) in 2012, it looks likely that the private sector will not make up for the negative impact of these austerity measures given the lack of an export led recovery due to the downturn in our major trading partner – the EU. The housing market, a gauge of consumer confidence, remains weak and the outlook is for house prices to be little changed for a prolonged period.

Economic Growth. GDP growth has, basically, flatlined since the election of 2010 and, worryingly, the economic forcecasts for 2012 and beyond have been revised lower on a near quarterly basis. With concerns of a potential return to recession, the Bank of England embarked on a second round of Quantitive Easing to stimulate economic activity. It appears very likely that there will be another expansion of quantitative easing in quarter 1 2012 in order to stimulate economic growth.

Unemployment. With the impact of the Government's austerity strategy resulting in steadily increasing unemployment during 2011, there are limited prospects for any improvement in 2012 given the prospects for weak growth.

Inflation and Bank Rate. For the last two years, the MPC's contention has been that high inflation was the outcome of temporary external factors and other one offs (e.g. changes in VAT); that view remains in place with CPI inflation starting quarter 1 of 2012 at 4.8%, having peaked at 5.2% in September 2011. They remain of the view that the rate will fall back to, or below, the 2% target level within the two year horizon.

AAA rating. The ratings agencies have recently reaffirmed the UK's AAA sovereign rating and have expressed satisfaction with Government policy for deficit reduction. They have, though, warned that this could be reviewed if the policy were to change, or was seen to be failing to achieve its desired outcome. This credit position has ensured that the UK government is able to fund itself at historically low levels and, with the safe haven status from Eurozone debt also drawing in external investment, the pressure on rates has been down, and looks set to remain so for some time.

(c) Sector's forward view

Economic forecasting remains troublesome with so many extermal influences weighing on the UK. There does, however, appear to be consensus among analysts that the economy remains weak and whilst there is still a broad range of views as to potential performance, they have all been downgraded throughout 2011. Key areas of uncertainty include:

- a worsening of the Eurozone debt crisis and heightened risk of the breakdown of the bloc or even of the currency itself;
- the impact of the Eurozone crisis on financial markets and the banking sector;
- the impact of the Government's austerity plan on confidence and growth and the need to rebalance the economy from services to exporting manufactured goods;
- the under-performance of the UK economy which could undermine the Government's policies that have been based upon levels of growth that inceasingly seem likely to be undershot;

- a continuation of high levels of inflation ;
- the economic performance of the UK's trading partners, in particular the EU and US, with some analysts suggesting that recession could return to both;
- stimulus packages failing to stimulate growth;
- elections due in the US, Germany and France in 2012 or 2013;

- potential for protectionism i.e. an escalation of the currency war / trade dispute between the US and China.

The overall balance of risks remains weighted to the downside. Lack of economic growth, both domestically and overseas, will impact on confidence putting upward pressure on unemployment. It will also further knock levels of demand which will bring the threat of recession back into focus.

Sector believes that the longer run trend is for gilt yields and PWLB rates to rise due to the high volume of gilt issuance in the UK, and the high volume of debt issuance in other major western countries.

Given the weak outlook for economic growth, Sector sees the prospects for any interest rate changes before mid-2013 as very limited. There is potential for the start of Bank Rate increases to be even further delayed if growth disappoints.

LOCAL GOVERNMENT INVESTMENTS (England)

SPECIFIED INVESTMENTS 2012/13

All "Specified Investments" listed below must be sterling-denominated.

Investment	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / Minimum Credit Rating **	Capital Expenditure?	Circumstance of use	Maximum period
Debt Management Agency Deposit Facility* (DMADF) * this facility is at present available for investments up to 6 months	No	Yes	Govt-backed	NO	In-house	1 year *
Term deposits with the UK government or with UK local authorities (i.e. local authorities as defined under Section 23 of the 2003 Act) with maturities up to 1 year	No	Yes	High security although LAs not credit rated.	NO	In-house	1 year
Term deposits with credit-rated deposit takers (banks and building societies), including callable deposits, with maturities up to 1 year	No	Yes	Yes-varied** Short-term F1or F1+, Individual A or B, Support 1,2,3 or equivalent	NO	In-house	1 year
Certificates of Deposit issued by credit-rated deposit takers (banks and building societies) : up to 1 year. *Custodial arrangement required prior to purchase*	No	Yes	Yes-varied** Short-term F1or F1+, Individual A or B, Support 1,2,3 or equivalent	NO	to be used in-house after consultation/ advice from Sector	1 year
Gilts : with maturities up to 1 year *Custodial arrangement required prior to purchase*	No	Yes	Govt-backed	NO	Buy and hold to maturity : to be used in-house after consultation/ advice from Sector	1 year

APPENDIX 4

LOCAL GOVERNMENT INVESTMENTS (England)

SPECIFIED INVESTMENTS 2012/13 (Continued)

All "Specified Investments" listed below must be sterling-denominated.

Investment	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / 'High' Credit Rating criteria	Capital Expenditure?	Circumstance of use	Maximum period
Money Market Funds (i.e. a collective investment scheme as defined in SI 2004 No 534) *These funds do not have any maturity date*	No	Yes	AAA	NO	In-house	*the period of investment may not be determined at the outset but would be subject to cash flow and liquidity requirements*
Treasury bills [*Government debt security with a maturity less than one year and issued through a competitive bidding process at a discount to par value*] *Custodial arrangement required prior to purchase*	No	Yes	Govt-backed	NO	In-house	1 year
Bonds issued by a financial institution that is guaranteed by the United Kingdom Government (as defined in SI 2004 No 534) with maturities under 12 months *Custodial arrangement required prior to purchase*	No	Yes	Govt-backed	No	Buy and hold to maturity : to be used in-house after consultation/ advice from Sector	1 year
Bonds issued by multilateral development banks (as defined in SI 2004 No 534) with maturities under 12 months *Custodial arrangement required prior to purchase*	No	Yes	AAA	No	Buy and hold to maturity : to be used in-house after consultation/ advice from Sector	1 year

**Minimum credit ratings

LOCAL GOVERNMENT INVESTMENT (England)

NON-SPECIFIED INVESTMENTS 2012/13

Investment	(A) Why use it? (B) Associated risks?	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / Minimum credit rating **	Capital Expend iture?	Circumstance of use	Max Investment	Maximum maturity of investment
Term deposits with credit rated deposit takers (banks and building societies) with maturities greater than 1 year	(A) (i) Certainty of rate of return over period invested. (ii) No movement in capital value of deposit despite changes in interest rate environment. (B) (i) Illiquid : as a general rule, cannot be traded or repaid prior to maturity. (ii) Return will be lower if interest rates rise after making the investment. (iii) Credit risk : potential for greater deterioration in credit quality over longer period	No	No	YES-varied** long-term AA- or better, Individual A or B, Support 1,2 or equivalent	NO	in-house	£3m any one counterparty AND £3m in total	3 years
Certificates of Deposit with credit rated deposit takers (banks and building societies) with maturities greater than 1 year *Custodial arrangement required prior to purchase*	(A) (i) Although in theory tradable, are relatively illiquid. (B) (i) 'Market or interest rate risk' : Yield subject to movement during life of CD which could negatively impact on price of the CD.	No	Yes	YES-varied ** long-term AA- or better, Individual A or B, Support 1,2 or equivalent	NO	to be used in-house after consultation/ advice from Sector	£3m	3 years
Fixed Term Deposits with variable rates and variable maturities with credit rated deposit takers (banks and building societies) with maturities greater than 1 year	(A) (i) Enhanced income ~ Potentially higher return than using a term deposit with similar maturity. (B) (i) Illiquid – only borrower has the right to pay back deposit; the lender does not have a similar call. (ii) period over which investment will actually be held is not known at the outset. (iii) Interest rate risk : borrower will not pay back deposit if interest rates rise after deposit is made.	No	No	YES-varied ** long-term AA- or better, Individual A or B, Support 1,2 or equivalent	NO	to be used in-house after consultation/ advice from Sector	£3m	3 years in aggregate

LOCAL GOVERNMENT INVESTMENT (England)

NON-SPECIFIED INVESTMENTS 2012/13 (Continued)

Investment	(A) Why use it? (B) Associated risks?	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / Minimum credit rating **	Capital Expend iture?	Circumstance of use	Max % of overall investments	Maximum maturity of investment
UK government gilts with maturities in excess of 1 year *Custodial arrangement required prior to purchase*	(A) (i) Excellent credit quality. (ii)Very Liquid. (iii) If held to maturity, known yield (rate of return) per annum ~ aids forward planning. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (v) No currency risk (B) (i) 'Market or interest rate risk' : Yield subject to movement during life of sovereign bond which could negatively impact on price of the bond i.e. potential for capital loss.	No	Yes	Govt backed	NO	Buy and hold to maturity : to be used in-house after consultation/ advice from Sector	£3m	maturity limit 5 years
Sovereign issues ex UK govt gilts : any maturity *Custodial arrangement required prior to purchase*	(A) (i) Excellent credit quality. (ii) Liquid. (iii) If held to maturity, known yield (rate of return) per annum ~ aids forward planning. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (v) No currency risk (B) (i) 'Market or interest rate risk' : Yield subject to movement during life of sovereign bond which could negatively impact on price of the bond i.e. potential for capital loss.	No	Yes	AAA	NO	Buy and hold to maturity : to be used in-house after consultation/ advice from Sector	£3m	5 years

LOCAL GOVERNMENT INVESTMENT (England)

NON-SPECIFIED INVESTMENTS 2012/13 (Continued)

Investment	(A) Why use it? (B) Associated risks?	Share/ Loan Capital?	Repayable/ Redeemable within 12 months?	Security / Minimum credit rating **	Capital Expenditure ?	Circumstance of use	Max % of overall investments	Maximum maturity of investment
Bonds issued by a financial institution that is guaranteed by the United Kingdom Government (as defined in SI 2004 No 534) with maturities in excess of 1year *Custodial arrangement required prior to purchase*	(A) (i) Excellent credit quality. (ii) relatively liquid. (although not as liquid as gilts) (iii) If held to maturity, known yield (rate of return) per annum, which would be higher than that on comparable gilt ~ aids forward planning, enhanced return compared to gilts. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (B) (i) 'Market or interest rate risk' : Yield subject to movement during life of bond which could negatively impact on price of the bond i.e. potential for capital loss. (ii) Spread versus gilts could widen	Yes	Yes	AAA / government guaranteed	NO	Buy and hold to maturity : to be used in-house after consultation/ advice from Sector	£3m	5 years
Bonds issued by multilateral development banks (as defined in SI 2004 No 534) with maturities in excess of 1 year *Custodial arrangement required prior to purchase*	(A) (i) Excellent credit quality. (ii) relatively liquid. (although not as liquid as gilts) (iii) If held to maturity, known yield (rate of return) per annum, which would be higher than that on comparable gilt ~ aids forward planning, enhanced return compared to gilts. (iv) If traded, potential for capital gain through appreciation in value (i.e. sold before maturity) (B) (i) 'Market or interest rate risk' : Yield subject to movement during life of bond which could negatively impact on price of the bond i.e. potential for capital loss. (ii) Spread versus gilts could widen	Yes	Yes	AAA or government guaranteed	NO	Buy and hold to maturity : to be used in-house after consultation/ advice from Sector	£3m	5 years

* **The prohibition on the use of derivatives** : This prohibition effectively relies on the judgement of the House of Lords in the case of Hazell v The Council of the London Borough of Hammersmith and Fulham and Others in 1991. Their Lordships held that local authorities have no power to enter into interest rate swaps and similar instruments.
Sector believes that as this ruling still stands and will not be rescinded by the introduction of the Local Government Act 2003, local authorities will not have the power to use derivative instruments.

** minimum credit rating

APPENDIX 5

APPROVED COUNTRIES FOR INVESTMENT

AAA

- Australia
- Canada
- Denmark
- Finland
- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland
- UK

AA+

- France
- Hong Kong
- USA

AA

- Belgium
- UAE

AA-

- Japan
- Qatar
- Saudi Arabia