Treasury Management Strategy 2014/15

Background

In accordance with the Council's Treasury Management Practices (TMPs) and The Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services: Code of Practice the Council is required to approve the Treasury Management Strategy and Annual Investment Strategy for 2014/15. The Treasury Management Strategy is reflected in the Personal Assurance Statement given by the Director of Resources concerning the 2014/15 budget calculations.

Treasury management is undertaken by a small team of professionally qualified staff within the Resources Directorate.

In addition the Council employs Treasury Management advisors, Arlingclose, who provide information and advice on interest rate movements which is used to inform borrowing and investment decisions. The advisors have been engaged on a fixed term basis after a tendering procedure that concluded in July 2013.

Relevant information is also obtained from other financial commentators, the press and seminars arranged by other organisations, for example CIPFA and the Local Government Association.

Information received from these different sources is compared in order to ensure all views are considered and there are no significant differences or omissions from information given by the Council's advisors.

All Treasury Management employees take part in the Council's Staff Review and Development scheme, where specific individual training needs are highlighted training in Treasury Management activities and networking opportunities provided by both professional and commercial organisations are taken up where appropriate.

During 2013/14 the County Council has invested its surplus cash with selected UK Banks, selected Money Market Funds, the UK Debt Management Office and with other local authorities.

Economic Commentary

During 2013 there has been an improvement in business and consumer sentiment.

2013 has seen the strongest growth of any calendar year since the banking crisis, with growth of 0.4% in Q1, 0.7% in Q2 and 0.8% in Q3. However the slow increase in employment and continued weakness in the Eurozone, where the UK does much of its trade, is likely to counter growth accelerating further.

Inflation continues to moderate, with the CPI for November 2013 coming in at 2.1%, only just above the Bank of England's 2% target. Lower transport costs have been the key driver behind the recent fall. Higher energy costs in the pipeline are expected to put upward pressure on inflation in the immediate future. However if inflation continues to moderate, then real household incomes may begin to rise for the first time in a number of years, aiding consumer spending. CPI in December was
2.0%

Activity in the US continues to pick-up at a higher rate still than the UK, with the prospect of tightening monetary policy during 2014. The continued stand-off between the White House and Congress over the budget is a concern however.

The Eurozone economies continue to lag behind the recovery seen elsewhere, with renewed concern over France's economy outweighing an improving situation in Ireland and Spain. On the positive side agreement is close on a new banking resolution mechanism that will lessen the impact on taxpayers of any future banking crises.

The UK bank base rate has remained at the historically low level of 0.5% throughout the year. The Bank of England, under its new governor Mark Carney, has issued forward guidance which sets out the conditions under which the Bank of England will consider tightening Monetary Policy again. One key measure is the unemployment rate falling back to 7% or lower. The Bank's own forecasts suggest that the base rate should not increase until Q4 2016, in spite of recent data and market expectations for an increase in Q4 2014.

Bank of England forward guidance is not set in stone and it can be altered if the recovery stalls, or if inflation becomes an issue again.

The Council's Treasury Management Advisors, Arlingclose agree with the Bank of England's forecasts for the base rate to remain at 0.5% until Q4 2016. They have stated there are upside risks to this forecast though and these increase towards the end of the forecast period.

In November 2012, the Public Works Loans Board (PWLB) launched the new "Certainty rate", which in exchange for summary information of the council's medium-term borrowing plans being submitted to HM Treasury, has given the council access to borrowing rates of 0.2% below those which would otherwise be available over all maturity periods. Rates applicable to early repayment of debt remain the same with the difference between these two sets of rates such that opportunities to reschedule debt are considerably limited.

Treasury Management Strategy

The Prudential Code for Capital Finance requires the Council to set a number of Prudential Indicators. The Treasury Management Strategy has been developed in accordance with these indicators.

Borrowing Strategy

The outlook for borrowing rates is currently difficult to predict. Fixed interest borrowing rates are based on UK gilt yields, which due to a recovering economy, have increased in recent months and are expected to continue to do so over the medium term. This is due to investors being more comfortable investing in riskier assets and selling gilts to seek higher returns.

The Council's Treasury Management advisors have produced forecasts which suggest that rates over all periods of borrowing will increase slowly during 2014/15, and continue to do so in future years. Rates on loans of 5 years are forecast to be around 2.5% while rates on longer term loans are expected to be around 4.5% by the end of 2014/15.

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with external debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure.

The strategy will be to borrow in order to replenish a proportion of the reserves and cash balances used to support capital expenditure since October 2008. This will mitigate any interest rate risk in that borrowing and will be taken before borrowing rates increase significantly. The timing of the borrowing will depend on cashflow requirements and forecast future developments and on interest rate movements and the forecast for those future movements. A mixture of shorter and longer-term loans will be taken in order to fit with the Council's debt maturity profile.

Interest rates will be monitored but as forecasts stand it is likely that borrowing will be undertaken towards the final third of the financial year.

The gross capital borrowing requirement for 2014/15 is estimated to be £53.9 million. After the use of the minimum revenue provision to repay debt of £16.8 million, the net capital borrowing requirement is estimated to be £37.1 million.

The management of the Council’s debt will be exercised in the most efficient manner taking into account maturing debt. The opportunity will be taken to reschedule any outstanding debt if rates are favourable, and make savings in the revenue budget. The cost of external interest of maintaining the council debt is estimated to be £15.1 million in 2014/15.

In addition to its usual borrowing activity, the Council will be undertaking a project with Mercia Waste, to provide finance for the construction of an Energy Plant. Further details are given below in the paragraph titled "Energy from Waste".

Annual Investments Strategy

The Council's Investment Strategy has been drawn up having regard to both the Communities and Local Government's Guidance on Local Authorities Investments and the CIPFA Treasury Management in Public Services Code of Practice and CIPFA Cross-Sectoral Guidance Notes. This strategy will be revised and presented to Council if changes occur outside those envisaged within this strategy.

The policy objective for the Council is the prudent investment of its cash balances. The investment priorities are firstly the security of capital (protecting sums from capital loss) and secondly the liquidity of investments (ensuring cash is available when required). Only when these two priorities are met will the third, of achieving the optimum return on investments, be taken into account.

The Council will not borrow money purely to invest. The Council will only borrow up to 12 months in advance of cash being required to fund its capital expenditure and the amount borrowed will not exceed the annual borrowing requirement.

The investments, which the Council are able to use for the prudent management of cash balances are categorised as ‘Specified Investments’ and ‘Non-Specified Investments’.

A Specified Investment offers high security and high liquidity, must be in sterling and have a maturity date of less than a year. Any Specified Investment must be with the United Kingdom Government, a local authority in England or Wales or a similar body in Scotland or Northern Ireland, a parish or community council, a AAA rated Moneymarket Fund, a bank which is part-owned by the UK Government, or with a body of high credit quality. The Council defines a body of high credit quality as counterparties who achieve ratings with all three rating agencies as described in the table below.

Agency:	**Long-Term:**	**Short Term:**
Fitch	AA	F1+
Moodys	Aa2	P-1
Standard and Poors	AA	A-1+

Non Specified Investments have a range of vehicles not covered by the definition of Specified Investments, which are set out in the Treasury Management Practices (TMPs) and generally carry more risk. Only investments where there is no contractual risk to the capital invested and where the rate of return justifies their use will be entered into. The only category of Non Specified investment identified for use for the coming financial year is a routine term investment with a counterparty as described above for Specified Investments, for a period of more than one year. This type of investment will be considered when rates are favourable and cash balances allow. The Council’s prudential indicators allow no more than £5 million to be invested in this category.

The credit ratings of Fitch, Moodys and Standard and Poors are monitored at least weekly, ratings watches and downgrades are acted upon immediately. Any other information that is deemed relevant to the creditworthiness of any Counterparty will be acted upon, in line with the revised code issued in 2009.

During 2013, the Council changed its banking services provider to Barclays and it may hold cash within its current account overnight as a transactional control to mitigate against the risk of going overdrawn and incurring penalty and interest charges. On limited occasions the Council may also leave funds in this account when the amounts involved are too small to invest elsewhere economically or practically. These balances are considered as cash or cash equivalents and not investments.

The Council will aim to have not less than 50% of its investments returnable within 28 days with at least 20% within 7 days.