

Audit Committee – 23rd February 2012

7. Treasury Management Strategy Statement and Investment Strategy 2012/13

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Purpose of the Report

This report has been prepared for Audit Committee who has been tasked with the scrutiny of treasury management and to recommend to full Council the Treasury Management Strategy Statement and Investment Strategy for 2012/13.

Recommendation

To recommend the Treasury Management Strategy Statement and Investment Strategy for 2012/13 to full Council;

Background

The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators on an annual basis.

CIPFA has defined Treasury Management as:

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

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

- Liquidity Risk (Adequate cash resources)
- Market or Interest Rate Risk (Fluctuations in the value of investments).
- Inflation Risks (Exposure to inflation)
- Credit and Counterparty Risk (Security of Investments)
- Refinancing Risks (Impact of debt maturing in future years).
- Legal & Regulatory Risk (Compliance with statutory and regulatory requirements).

The Local Government Act 2003 requires the Council to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable. The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy; this sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

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The proposed strategy for 2012/13 takes into account the Council's current treasury position and the approved Prudential Indicators and draws upon the forecasts for interest rates provided by the Council's treasury advisers.

The Strategy is attached at Appendix 1 (pages 19-47) and is split into the following main areas:

- Background
- Balance Sheet and Treasury Position
- Outlook for Interest Rates
- Borrowing Requirement and Strategy
- Investment Policy and Strategy
- Balanced Budget Requirement
- 2012/13 MRP Statement
- Reporting
- Other Items

Changes

The major changes within the strategy are in response to changes in the CLG Guidance and evolving conditions in financial markets. This means that from 1st April 2012, accounting for any corporate bonds purchased after this date will be on a non-capital investment basis.

However, the principal amendments are in relation to the individual institutions to whom the Authority is prepared to lend funds. The Authority and its advisors - Arlingclose Ltd, select countries and financial institutions based on analysis and ongoing monitoring of:

- Published credit ratings for financial institutions (minimum long term rating of A- or equivalent for counterparts; AA+ or equivalent for non UK sovereigns). This is lower than the A+ minimum adopted in 2011/12 and is in response to downgrades in credit ratings below A+ of many institutions considered to be systemically important to the financial system
- Credit Default Swaps (where quoted)
- Economic fundamentals (for example Net Debt as a percentage of GDP)
- Sovereign support mechanisms
- Share Prices
- Corporate developments, news, articles, markets sentiment and momentum
- Subjective overlay

By reducing the minimum long term rating of A- or equivalent the following types of investments can be made with the respective rates of returns

| | |
|--------------------------------|--------|
| Treasury Bill | 0.356% |
| DMADF | 0.250% |
| High Street Bank A+ (HSBC) | 0.300% |
| High Street Bank A- (Barclays) | 0.970% |
| Other Local Authority | 0.370% |

Financial Implications

The revised strategy will achieve the budget for new investments in 2013/14. If members would prefer to accept a more risk averse strategy we will be unable to achieve the Treasury Management Interest budget because the Authority will be restricted to counterparties who offer lower rates of return. In addition, there would be less diversification within the Council's portfolio, ultimately concentrating all risks within a select few counterparties.

Background Papers: *Cipfa Treasury Management Code of Practice*
Arlingclose Technical Paper – Revisions to the TM Code and Prudential Code
Treasury Management Practices
