BOROUGH OF POOLE

CABINET

5 FEBRUARY 2008

TREASURY MANAGEMENT STRATEGY STATEMENT 2008/2009

PART OF PUBLISHED FORWARD PLAN: YES

STATUS – STRATEGIC POLICY

1. Purpose & Policy Context of Report

1.1 The purpose of this report is to present to Members the Treasury Management Strategy Statement for the 2008/2009 financial year which is required annually by the Council's Treasury Management Policy.

2. Decisions Required

2.1 That the 2008/2009 Treasury Management Strategy be approved.

3. Background

3.1 The Council adopted the latest CIPFA Treasury Management Code of Practice with effect from 1 April 2002. The Code sets out a framework of operating procedures for Members and Officers to reduce treasury risk and improve dialogue about the Council's Treasury position. Treasury management is defined 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."

3.2 The production of a Treasury Management Strategy Statement details the expected activities of the Treasury function in the forthcoming 2008/2009 financial year. The proposed strategy is based upon existing policies and approved strategies including the Council's Medium Term Financial Plan as well as the Head of Financial Services views on interest rates, supplemented with market forecasts from a variety of sources.

3.3 **The report covers:**

i. The current treasury position;
ii. Prudential system (including Prudential Indicators);
iii. The objectives of the strategy;
iv. Prospects for interest rates;
v. 2008/2009 strategy;
vi Approved organisations for investments;

vii. Minimum Revenue Provision (MRP).

4. Current Treasury Position (January 2008)

4.1 The Council's current average cash investment balance for 2007/2008 is £41.4m.

4.2 The estimated average investment interest rate return in 2007/2008 is 5.6%.

4.3 The Council currently holds £32m of external long-term borrowing at an average fixed-interest rate of 4.6%.

5. Prudential System

5.1 The CIPFA Prudential Code requires a number of prudential indicators to be compiled. These are attached to this report.

5.2 With regard to Treasury Management the following indicators are relevant

i. Authorised Limit - The authorised limit sets a parameter for the level of affordable debt. It should not be set so high that it would never in any possible circumstances be breached. It should reflect a level of borrowing which, while not desired, could be afforded but may not be sustainable. In this way it may include provision for additional borrowing that may be required for a short period in order to deliver the agreed treasury management strategy.

ii. Operational Boundary -This indicator is the focus of day-to-day treasury management activity within the authority. It is a means by which the authority manages its external debt to ensure that it remains within the self-imposed authorised limit.

iii. Interest Rate Exposure – This indicator sets out the maximum level of borrowing, as a proportion of total borrowing, that would be taken out at variable or fixed rates.

iv. Fixed Rate Debt Maturity Structure – This indicator sets out the maximum levels of borrowing, as a proportion of total borrowing, that would be taken out over different maturity profiles.

6. Objectives of the Strategy

6.1 The major objectives to be followed in 2008/2009 are:

(a) Borrowing

i) To minimise the revenue costs of debt commensurate with exposure to future risk

ii) To manage the Council's debt maturity profile i.e. to leave no one future year with a disproportionately high level of debt principal repayments that could lead to difficulties in terms of re-borrowing

iii) To borrow in accordance with forecasted average future interest rates, (i.e., short term and/or variable when rates are ‘high’, long term and fixed when rates are ‘low’. Similarly, maturity loans can be taken when rates are relatively low, to lock in the principal for the maximum period, annuity loans and equal instalments of principal loans when rates are considered higher).

iv) To monitor and review the level of variable interest rate loans in order to take advantage of future forecasted interest rate movements

(b) *Investment*

i) The Council’s investment priority is to maintain the **security** of capital

ii) To maintain policy flexibility through **liquidity** of its investments

iii) The Council will aim to achieve the **optimum return** on its investments commensurate with the proper levels of security and liquidity.

7. Prospects for Interest Rates 2008/2009

7.1 **Shorter-term –** The Bank of England most recently changed its current Base Rate to 5.5% on 6 December 2007. According to the latest market data available, opinions are divided on the future of Base Rate over the next few months, the most likely scenario is that Base Rate will reduce to 5% by the middle of the year although some commentators say that the rate will remain unchanged with others suggesting that it will fall to 4.5%. The Monetary Policy Committee (MPC) is required to achieve a target of 2.0% Consumer Prices Index (CPI) inflation, subject to a margin of 1.0% on either side. November’s CPI inflation was 2.1%, which was unchanged from October.

7.2 **Longer-term -** PWLB rates for periods of 10 to 25 years fell slightly at end of 2007.

8. The Strategy for 2008/2009

Capital finance

8.1 To consider the use of supported borrowing, to use all usable capital receipts and maximise the use of capital grants.

Borrowing

8.2 The Council took out £10m new long-term borrowing in August 2007 in order to meet its capital programme funding requirements.

8.3 Whilst there is clearly a longer term requirement to undertake significant borrowing in support of both the General Fund and HRA capital programme, the Head of Financial Services will continue to monitor cash balances over the medium term and to consider long-term fixed rate borrowing at a point that is considered favourable to the Council.

Temporary investments

8.5 The Council will continue to invest its temporary surplus funds prudently in accordance with its Treasury Management Policy. Priority is to be given to security and liquidity rather than yield. It is reasonable to seek the highest rate of interest consistent with the proper levels of security and liquidity.

8.6 In response to the volatility in the financial markets, which manifested itself via the liquidity crisis in the money markets and the Bank of England stepping in to support Northern Rock, the Head of Financial Services has tightened the Council's current lending criteria for 2007/08 and 2008/09. This action, whilst improving the security of the Council's investments has inevitably led to a reduction in the potential yield.

8.7 Currently the Council will only lend to UK based financial institutions with, as a minimum, a double A long term credit rating or other Local Authorities.

8.8 The Head of Financial Services will continue to monitor the situation and take all reasonable steps to protect the Council's investments.

9. Approved Organisations for Investment

9.1 The Head of Financial Services will continue to construct the Council's lending list on the basis of up-to-date, internationally recognised Fitch IBCA credit ratings. All credit ratings will be monitored monthly.

10. Minimum Revenue Provision (MRP)

10.1 The Council is statutorily obliged to charge to the revenue account an amount to provide for the repayment of debt. The calculation of this amount follows a prescribed formula. The Department of Communities and Local Government (CLG) are consulting local authorities on changes to this mechanism which give 4 options on how to calculate the provision. They have suggested that Council's formally approve the policy it has adopted in calculating its provision.

10.2 The two options that are being recommended are those currently undertaken and are set out below. This recommendation is a formality and does not change the current financial provision made.

i. Approach 1: Regulatory Method

MRP is equal to the amount determined in accordance with the former regulations 28 and 29 of the 2003 Regulations, as if they had not been revoked by the 2008 regulations.

ii. Approach2 : Asset Life Method

Where capital expenditure on an asset is financed wholly or partly by borrowing or credit arrangements, MRP is to be made in equal annual installments over the life of the asset, in accordance with the following formula:

$$\frac{\mathbf{A - B}}{\mathbf{C}}$$

where-
A is the amount of the capital expenditure in respect of the asset financed by borrowing or credit arrangements
B is the total provision made before the current financial year in respect of that expenditure
C is the inclusive number of financial years from the current year to that in which the estimated life of the asset expires.
This does not preclude the repayment over a shorter period than the life of the asset.

11. Financial and Legal Implications

11.1 Financial implications are as outlined within the report.

11.2 There are no legal implications.

BOB JACKSON
HEAD OF FINANCIAL SERVICES

Background Papers
Nil

Name and Telephone Number of Officer Contact
Martin Moore, 01202-633397
7 January 2008