MEETING:	**FULL COUNCIL**
DATE:	**1 MARCH 2012**
TITLE:	**TREASURY MANAGEMENT:** **i) REVISION OF THE TREASURY MANAGEMENT POLICY STATEMENT FOLLOWING PUBLICATION OF A REVISED CODE BY CIPFA** **ii) TREASURY MANAGEMENT STRATEGY STATEMENT, MINIMUM REVENUE PROVISION STRATEGY AND ANNUAL INVESTMENT STRATEGY FOR 2012/13**
PURPOSE:	**ADOPT THE POLICY AND PROPOSED STRATEGIES**
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PORTFOLIO LEADER:	**COUNCILLOR SIÂN GWENLLIAN**

1. CODE OF PRACTICE

The Code of Practice for managing Treasury Management in the Public Services published by CIPFA, requires the Council to prepare a Policy Statement and practice papers together with detailed schedules setting out the Council's approach to all treasury operations. The primary requirement of the Code is the approval by the Full Council of the Policy Statement, the practice papers and the schedules. These were approved by the Council at its meeting of 3rd March 2011. Following a further review in November 2011, CIPFA now requires the Policy Statement to include the Council’s high level policies for borrowing and investments. The revised Policy Statement is detailed herewith as **Appendix A.**

2. INVESTMENT STRATEGY

The Welsh Assembly Government's Statutory Guidance on Local Government Investments ("The Guidance"), requires the Council, as part of its treasury management function to prepare an Annual Investment Strategy. The Guidance states that authorities can combine the Treasury Management Strategy Statement and the Annual Investment Strategy into one report. The Council has adopted that suggestion and the Annual Investment Strategy is therefore included as section 7 of **Appendix B.**

3. TREASURY MANAGEMENT STRATEGY

The Council is required by the Code and the Guidance to approve an annual Treasury Management Strategy Statement, Minimum Revenue Provision Strategy and an Annual Investment Strategy prior to the commencement of each financial year. The proposed strategy for 2012/13 is detailed herewith as **Appendix B.**

4. PRUDENTIAL INDICATORS

In addition the Local Government Act 2003 introduced a new prudential framework for local authority's capital investment. The new arrangements, which were applicable from 1st April 2004 introduced a new system of governance for local authority capital expenditure, based largely on self regulation. The Prudential Code for Capital Finance in Local Authorities has been developed by CIPFA as a professional code of practice, with statutory backing, to support local authorities in taking these decisions. Key objectives are to ensure that the capital investment plans of local authorities are affordable, prudent and sustainable. Local authorities, before the beginning of each financial year, are required to set certain prudential indicators for the forthcoming and following years. Following the recent review, CIPFA has now introduced a new prudential indicator, "Upper limits on the proportion of net debt to gross debt" to highlight where an authority may be borrowing in advance of its cash requirement. The indicators which are based on the capital and revenue budget proposals contained elsewhere on the agenda are shown in **Appendix C**.

5. COUNTERPARTIES (BANKS)

The counterparty list **(Appendix CH)** has been updated to reflect the latest recommendations. The maximum length of loans to UK Institutions have been lowered from 2 years to 1 year to reflect these recommendations. These changes are noted in bold print on the list of Authorised Counterparties in **Appendix CH** with the previous limits shown in brackets.

6. BORROWING

With effect from 31st March 2008, the Welsh Assembly Government introduced the Local Authorities (Capital Finance and Accounting) (Wales) (Amendment) Regulations 2008 [the "Amendment Regulations"]. These Regulations introduce certain amendments to those introduced in 2003 [the "Original Regulations"] as part of the implementation of the Prudential Borrowing regime. Amongst the changes introduced is the requirement for an Annual Minimum Revenue Provision (MRP) Policy Statement. The Original Regulations set out a statutory basis and a complex formula for the calculation of MRP. The Amendment Regulations only require a charge that is 'prudent', and authorities are permitted more discretion in terms of the charge levied, albeit within certain parameters. The attached strategy in Section 11 of **Appendix B** therefore also incorporates the Annual MRP Statement for 2012/13.

7. MEMBERS' WORKSHOP

Members of the Audit Committee and the Finance Portfolio Leader were invited to a briefing meeting with Arlingclose, the Council's Treasury Advisors, to discuss Treasury Management. Members were reminded of CIPFA's Code of Practice for Treasury Management as well as their roles and responsibilities as members for the Treasury Management function. The advisors highlighted the various current treasury risks, and spoke in detail about the credit and counterparty risks, interest rate risks and inflation risk. They also discussed the Council's debt portfolio, the prudential indicators, as well as highlighting the main changes to the TM Code and Guidance Notes following CIPFA's revision in November 2011.

8. FORMAL SCRUTINY

All of the following papers were presented to the Audit Committee on 13 February and to the Council Board on 14 February, where it was explained that the threat to the UK's credit rating would not affect the content. The Audit Committee and Board decided to recommend to the full Council as follows:

RECOMMENDATION

9. The Council is asked to adopt the Treasury Management Policy Statement (Appendix A), Treasury Management Strategy Statement, MRP Strategy and the Annual Investment Strategy for 2012/13 (Appendix B), the Prudential Indicators (Appendix C) and the changes to the Treasury Management Schedules (Appendix CH).

APPENDIX A

GWYNEDD COUNCIL

TREASURY MANAGEMENT POLICY STATEMENT

1. This Council defines its treasury management activities as:

   "The management of the Council'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."

2. This 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. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council, and any financial instruments entered into to manage these risks.

3. This Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

4. The Council’s borrowing will be affordable, sustainable and prudent and consideration will be given to the management of interest rate risk and refinancing risk. The source from which the borrowing is taken and the type of borrowing should allow the Council transparency and control over its debt.

5. The Council’s primary objective in relation to investments remains the security of capital. The liquidity or accessibility of the Authority’s investments followed by the yield earned on investments remain important but are secondary considerations.

APPENDIX B

TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2012/13 TO 2014/15

1. Background

1.1 The CIPFA 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 (PIs) on an annual basis. The TMSS also includes the Annual Investment Strategy (AIS) that is a requirement of the Welsh Government's (WG's) Investment Guidance.

1.2 The purpose of this TMSS is, therefore, to approve:
- Treasury Management Strategy for 2012/13
- Annual Investment Strategy for 2012/13
- Prudential Indicators for 2012/13, 2013/14 and 2014/15
- MRP Statement.

1.3 Treasury Management is about the management of risk. The Authority is responsible for its treasury decisions and activity. No treasury management activity is without risk.

1.4 As per the requirements of the Prudential Code, the Authority has adopted the CIPFA Treasury Management Code at a meeting of its Full Council on 3rd March 2011.

1.5 All treasury activity will comply with relevant statute, guidance and accounting standards.

2. Capital Financing Requirement

2.1 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). The CFR, together with Usable Reserves, are the core drivers of the Authority's Treasury Management activities.

2.2 The Authority's current level of debt and investments is shown below:

	23 January 2012 £m
External Borrowing:	
Fixed Rate – PWLB	97.8
Fixed Rate – Market	16.2
IFRS Long-term Liabilities:	
Operating Leases	0.5
Total External Debt	**114.5**
Total Investments	**(70.9)**
Net Borrowing Position / (Net Investment Position)	**43.6**

2.3 The Authority is able to borrow funds in excess of the current level of its CFR up to the projected level in 2014/15. The Authority is likely to only borrow in advance of need if it felt the benefits of borrowing at interest rates now compared to where they are expected to be in the future, outweighs the current cost and risks associated with investing the proceeds until the borrowing was actually required.

2.4 The forecasted movement in the CFR in coming years is one of the Prudential Indicators (PIs). The movement in actual external debt and usable reserves combine to identify the Authority’s borrowing requirement and potential investment strategy in the current and future years.

Table 1: Balance Sheet Summary Analysis

	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Capital Financing Requirement (CFR)	153.80	162.03	170.34	173.50
Less: Existing Profile of Borrowing and Other Long Term Liabilities	(114.34)	(112.84)	(113.53)	(116.51)
Cumulative Maximum External Borrowing Requirement	**39.46**	**49.19**	**56.81**	**56.99**
Usable Reserves	63.14	58.88	57.65	57.13
Cumulative Net Borrowing Requirement/(Investments)	**(23.68)**	**(9.69)**	**(0.84)**	**(0.14)**

2.5 Table 1 shows that the capital expenditure plans of the Authority cannot be funded entirely from sources other than external borrowing.

3. Interest Rate Forecast

3.1 The economic and interest rate forecast as at December 2011, is provided by the Authority’s treasury management advisor, Arlingclose Ltd, and is shown below. The Authority will reappraise its strategies from time to time in response to evolving economic, political and financial events.

	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
Official Bank Rate													
Upside risk					0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Downside risk													
1-yr LIBID													
Upside risk	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	1.75	1.75	1.75	1.75	1.80	1.85	1.95	2.00	2.10	2.20	2.30	2.40	2.40
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
5-yr gilt													
Upside risk	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	1.30	1.35	1.40	1.50	1.60	1.70	1.80	2.00	2.10	2.30	2.40	2.50	2.50
Downside risk	-0.25	-0.25	-0.25	-0.25	-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	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	2.30	2.40	2.45	2.50	2.55	2.60	2.70	2.75	2.80	2.85	2.90	3.00	3.00
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-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	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	3.05	3.05	3.10	3.20	3.25	3.30	3.35	3.40	3.45	3.50	3.60	3.75	3.75
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
50-yr gilt													
Upside risk	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central case	3.40	3.50	3.60	3.70	3.80	3.90	4.00	4.00	4.00	4.10	4.20	4.25	4.25
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25	-0.25

Their economic forecast at December 2011 is as follows:

- Conventional monetary policy has become largely redundant; the Bank of England and the US Federal Reserve have signalled their respective official interest rates will be on hold through to the end of 2012. We think that it could be 2016 before official UK interest rates rise.
- The UK's safe haven status, the direct effect of QE and minimal prospect of an increase in policy rates are expected to keep gilt yields at their lows in the near term.
- A disorderly outcome to the Eurozone sovereign crisis remains a key economic, credit and political risk.

Their underlying assumptions are as follows:

- Financial market stress is expected to remain a feature of 2012. Rates within Interbank markets (where banks fund the majority of their day to day operations) have continued to climb. This dynamic was a characteristic of the 2008 banking crisis and whilst the authorities have flooded the markets with liquidity, it is still a strong indicator of market risk.
- Inflation has moderated back to 4.8% in November. CPI is expected to drop gradually back towards the 2% target as the January 2011 VAT increase, the surge in oil prices and the large energy price hikes fall out of the twelve month comparison.
- Recent data and surveys suggest that since the summer the UK economy has lost the admittedly fragile momentum. Business and consumer surveys point to continued weakness in coming months. Public spending cuts, austerity measures, credit constraints, low business and consumer confidence could result in the economy stalling (Q3 excepted, when the 2012 Olympics will provide a temporary boost) and most likely pressure the Bank of England to provide further QE.
- Faltering global growth will not be helped by the considerable uncertainty and expansion of risks presented by the crisis in the Eurozone and gridlock in the US going into an election year. The knock-on effects could in turn weigh on growth in China and emerging market countries.
- Gilt supply is expected to be higher in 2012-13 than earlier forecast by the Treasury. However, over the short-term, gilts will retain their safe-haven status as euro area contagion risks grow.
- Sizeable European bond redemptions and refinancing (Italy in particular) in the first half of 2012 remain significant challenges. Headwinds to fiscal convergence and treaty changes could intensify downgrade pressures on the AAA core nations as well as peripheral countries. The effectiveness of the European Financial Stability Fund (EFSF) may prove limited, increasing the possibility of a sovereign failure or the break-up of the euro area.

4. Borrowing Strategy

4.1 Treasury management and borrowing strategies in particular continue to be influenced not only by the absolute level of borrowing rates but also the relationship between short and long term interest rates. The interest rate forecast shown in 3.1 above indicates that an acute difference between short and longer term interest rates is expected to continue. This difference creates a “cost of carry” for any new longer term borrowing where the proceeds are temporarily held as investments because of the difference between what is paid on the borrowing and what is earned on the investment. Whilst the cost of carry can be assumed to be a reasonably short-term issue since borrowing is often for longer dated periods (anything up to 50 years) it cannot be ignored against a backdrop of uncertainty and affordability constraints in the Authority’s wider financial position.

4.2 As indicated in Table 1, the Authority has a gross borrowing requirement of £49m in 2012/13 but has sufficient balances and reserves to avoid the need for external borrowing. By essentially lending its own surplus funds to itself the Authority is able to minimise borrowing costs and reduce overall credit and counterparty risk by reducing the level of its external investment balances.

5. Sources of Borrowing and Portfolio implications

5.1 In conjunction with advice from its treasury advisor, Arlingclose Ltd, the Authority will keep under review the following borrowing sources:

- PWLB
- Local authorities
- Commercial banks
- European Investment Bank
- Money markets
- Capital markets (stock issues, commercial paper and bills)
- Structured finance
- Leasing

5.2 The cost of carry has resulted in an increased reliance upon shorter dated and variable rate borrowing. This type of borrowing injects volatility into the debt portfolio in terms of interest rate risk but is counterbalanced by its affordability and alignment of borrowing costs with investment returns. The Authority's exposure to shorter dated and variable rate borrowing is kept under regular review by reference to the difference or spread between variable rate and longer term borrowing costs. A narrowing in the spread by 0.5% will result in an immediate and formal review of the borrowing strategy to determine whether the exposure to shorter dated and variable rates is maintained or altered.

5.3 The Authority has £16.2m exposure to LOBO loans (Lender's Option Borrower's Option) which can be "called" within 2013/14. A LOBO is called when the Lender exercises its right to amend the interest rate on the loan at which point the Borrower can accept the revised terms or reject them and repay the loan. LOBO loans present a potential refinancing risk to the Authority since the decision to call a LOBO is entirely at the lender's discretion. Any LOBOs called will be discussed with the treasury advisers prior to acceptance of any revised terms. The default position will be the repayment of the LOBO without penalty i.e. the revised terms will not be accepted. Based on the Balance Sheet summary at Table 1, new external borrowing would ultimately be required to fund any potenial repayment.

6. Debt Rescheduling

6.1 The Authority's debt portfolio can be restructured by prematurely repaying loans and refinancing them on similar or different terms to achieve a reduction in risk and/or savings in interest costs.

6.2 The lower interest rate environment and changes in the rules regarding the premature repayment of PWLB loans has adversely affected the scope to undertaken meaningful debt restructuring although occasional opportunities arise. The rationale for undertaking any debt rescheduling would be one or more of the following:

- Savings in risk adjusted interest costs;
- Rebalancing the interest rate structure of the debt portfolio;
- Changing the maturity profile of the debt portfolio.

6.3 Borrowing and rescheduling activity will be reported to the Audit Committee in the Annual Treasury Management Report and the regular treasury management reports presented to the Audit Committee.

7. Annual Investment Strategy

7.1 In accordance with Investment Guidance issued by the Welsh Government and best practice this Authority's primary objective in relation to the investment of public funds remains the security of capital. The liquidity or accessibility of the Authority's investments followed by the yields earned on investments is important but are secondary considerations.

7.2 Credit markets remain in a state of distress as a result of the excessive and poor performing debt within the financial markets. In some instances, Greece and Italy being the most notable examples, the extent and implications of the debt it has built up have lead to a sovereign debt crisis and a banking crisis with the outcome still largely unknown. It is against this backdrop of uncertainty that the Authority's investment strategy is framed.

7.3 Investments are categorised as "Specified" or "Non-Specified" within the investment guidance issued by the Welsh Government. Specified investments are sterling denominated investments with a maximum maturity of one year. They also meet the "high credit quality" as determined by the Authority and are not deemed capital expenditure investments under Statute. Non specified investments are, effectively, everything else.

7.4 The types of investments that will be used by the Authority and whether they are specified or non-specified are as follows:

Table 2: Specified and Non-Specified Investments

Investment	Specified	Non-Specified
Debt Management Account Deposit Facility	✓	✗
AAA rated Money Market Funds	✓	✗
Treasury Bills (T-Bills)	✓	✗
Local Authority Bills	✓	✗
Term deposits with other UK local authorities	✓	✓
Term deposits with banks and building societies	✓	✓
Certificates of deposit with banks and building societies	✓	✓
Gilts	✓	✓
Bonds issued by Multilateral Development Banks	✓	✓
Corporate Bonds	✓	✓
Other Money Market and Collective Investment Schemes	✓	✓
Business Loans to Local Companies (as agreed by the Local Loans Fund scheme)*	✗	✓

**Advancement of these loans will be approved by the procedure detailed below. Evaluation of the Business Loans is not part of the advice or services from the Authority's treasury advisor.*

7.5 A number of changes have been implemented to the investment strategy for 2012/13 in response to evolving conditions in financial markets. The credit crisis has refocused attention on the treasury management priority of security of the capital invested. The authority uses credit ratings to derive its list of counterparties. The authority and its treasury advisors, Arlinclose Ltd, will continue to maintain a counterparty list and will assess and update the credit standing of the institutions on a regular basis. The authority and its treasury advisors, select countries and financial institutions after analysis and ongoing monitoring of:

- Published credit ratings for financial institutions (minimum long term rating of A- or equivalent for counterparties; 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 – or, put more simply, common sense.

Any institution can be suspended or removed should any of the factors identified above give rise to concern. The council's counterparty list is shown in Appendix CH.

It remains the Authority's policy to make exceptions to counterparty policy established around credit ratings, but this is conditional and directional. What this means is that an institution that meets criteria may be suspended, but institutions not meeting criteria will not be added.

The Council has set up a Local Loans Fund which will make loans to local businesses. These investments are included in the Non-Specific Investments table above and will be for a maximum of 10 years. The total value of the fund for such investments will be £3million. Applications for loans under this scheme will not be part of the usual credit assessment for treasury management investment purposes but will be assessed by appointed consultants and any decision to lend will be made by the Investment Panel for the scheme.

7.6 Authority's Banker – The Authority banks with Barclays Bank plc. At the current time, it does meet the minimum credit criteria of A- (or equivalent) long term. Even if the credit rating falls below the Authority's minimum criteria it will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

8. Investment Strategy

8.1 With short term interest rates low for even longer, an investment strategy will typically result in a lengthening of investment periods, where cash flow permits, in order to lock in higher rates of acceptable risk adjusted returns. The problem in the current environment is finding an investment counterparty providing acceptable levels of counterparty risk.

8.2 In order to diversify an investment portfolio largely invested in cash, investments will be placed with a range of approved investment counterparties in order to achieve a diversified portfolio of prudent counterparties, investment periods and rates of return. Maximum investment levels with each counterparty will be set to ensure prudent diversification is achieved.

8.3 Money market funds (MMFs) will be utilised but good treasury management practice prevails and whilst MMFs provide good diversification the Authority will also seek to diversify any exposure by utilising more than one MMF. The Authority will also restrict its exposure to MMFs with lower levels of funds under management and will not exceed 0.5% of the net asset value of the MMF.

9. The Use of Financial Instruments for the Management of Risks

9.1 Currently, Local Authorities' legal power to use derivative instruments remains unclear. Consequently, the Authority does not intend to use derivatives.

9.2 Should this position change, the Authority may seek to develop a detailed and robust risk management framework governing the use of derivatives, but this change in strategy will require full Council approval.

10. Balanced Budget Requirement

10.1 The Authority complies with the provisions of S93 of the Local Government Finance Act 1992 to set a balanced budget.

11. 2012/13 MRP Statement

11.1 The Local Authorities (Capital Finance and Accounting)(Wales)(Amendment) Regulations 2008 (SI 2008/588 (W.59)) place a duty on local authorities to make a prudent provision for debt redemption. Guidance on Minimum Revenue Provision has been issued by the Welsh Ministers and local authorities are required to "have regard" to such Guidance under section 21(1B) of the Local Government Act 2003.

11.2 The four MRP options available are:
- Option 1: Regulatory Method
- Option 2: CFR Method
- Option 3: Asset Life Method
- Option 4: Depreciation Method

NB This does not preclude other prudent methods.

11.3 MRP in 2012/13: Options 1 and 2 may be used only for supported (i.e. financing costs deemed to be supported through Revenue Support Grant from Central Government) Non-HRA capital expenditure funded from borrowing. Methods of making prudent provision for unsupported Non-HRA capital expenditure include Options 3 and 4 (which may also be used for supported Non-HRA capital expenditure if the Authority chooses).

11.4 The MRP Statement will be submitted to Authority before the start of the 2012/13 financial year. If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement should be put to Authority at that time.

The Authority will apply Option 1 in respect of supported capital expenditure funded from borrowing and Option 3 in respect of unsupported capital expenditure funded from borrowing.

MRP in respect of leases and Private Finance Initiative schemes brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.

12. Monitoring and Reporting on the Treasury Outturn and Prudential Indicators

12.1 The Head of Finance will report to the Audit Committee on treasury management activity / performance and Performance Indicators as follows:

- six monthly against the strategy approved for the year. The Authority will produce an outturn report on its treasury activity no later than 30th September after the financial year end.
- the Audit Committee will be responsible for the scrutiny of treasury management activity and practices.

13. Other Items

13.1 Training

CIPFA's Code of Practice requires the Head of Finance to ensure that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Formal training, possibly sourced externally may be provided for relevant members during 2012/13.

Prudential Indicators 2012/13 – 2014/15

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.

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 the capital financing requirement in the preceding year plus the estimates of any additional increases to the capital financing requirement for the current and next two financial years.

The Head of Finance reports that the authority had no difficulty meeting this requirement in 2011/12, 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.

Capital Expenditure	2011/12 Approved £m	2011/12 Revised £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
General Fund	34.17	38.65	61.44	35.99	16.47
HRA	0.0	0.06	0.0	0.0	0.0
Total	**34.17**	**38.71**	**61.44**	**35.99**	**16.47**

3.2 Capital expenditure will be financed or funded as follows:

Capital Financing	2011/12 Approved £m	2011/12 Revised £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Capital receipts	3.74	4.20	1.89	2.09	2.10
Government Grants	7.30	15.66	31.13	15.55	2.46
Major Repairs Allowance	0	0	0	0	0
Revenue contributions	2.52	9.04	13.92	4.04	2.10
Total Financing	**13.56**	**28.90**	**46.94**	**21.68**	**6.66**
Supported borrowing	5.44	5.44	4.89	4.07	4.07
Unsupported borrowing	15.17	4.37	9.61	10.24	5.74
Total Funding	**20.61**	**9.81**	**14.50**	**14.31**	**9.81**
Total Financing and Funding	**34.17**	**38.71**	**61.44**	**35.99**	**16.47**

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 financing costs. The definition of financing costs is set out in the Prudential Code.

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

Ratio of Financing Costs to Net Revenue Stream	2011/12 Approved %	2011/12 Revised %	2012/13 Estimate %	2013/14 Estimate %	2014/15 Estimate %
General Fund	5.68	5.56	5.65	5.55	5.57
HRA	0	0	0	0	0
Total	**5.68**	**5.56**	**5.65**	**5.55**	**5.57**

5. Capital Financing Requirement:

5.1 The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and its financing.

Capital Financing Requirement	2011/12 Approved £m	2011/12 Revised £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
General Fund	164.22	153.80	162.03	170.34	173.50
HRA	0.0	0.0	0.0	0.0	0.0
Total CFR	**164.22**	**153.80**	**162.03**	**170.34**	**173.50**

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.

Actual External Debt as at 31/03/2011	£m
Borrowing	118.7
Other Long-term Liabilities	0.1
Total	**118.8**

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. 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.

Incremental Impact of Capital Investment Decisions	2011/12 Approved £	2012/13 Estimate £	2013/14 Estimate £	2014/15 Estimate £
Increase in Band D Council Tax	0.0	0.0	4.03	2.01

The increase in Band D council tax reflects the increases in the provision for Capital Financing Charges to undertake borrowing arising from the proposed capital programme.

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).

Authorised Limit for External Debt	2011/12 Approved £m	2011/12 Revised £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Borrowing	190.00	189.50	189.75	194.95	194.99
Other Long-term Liabilities	0.00	0.50	0.25	0.05	0.01
Total	**190.00**	**190.00**	**190.00**	**195.00**	**195.00**

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 Head of Finance 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. Any movement between these separate limits will be reported to the next meeting of the Council Board/Cabinet.

Operational Boundary for External Debt	2011/12 Approved £m	2011/12 Revised £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Borrowing	170.00	169.50	169.75	174.95	174.99
Other Long-term Liabilities	0.00	0.50	0.25	0.05	0.01
Total	**170.00**	**170.00**	**170.00**	**175.00**	**175.00**

9. Adoption of the CIPFA Treasury Management Code:

9.1 This indicator demonstrates that the Council has adopted the principles of best practice.

Adoption of the CIPFA Code of Practice in Treasury Management
The Council approved the adoption of the CIPFA Treasury Management Code at its full Council meeting on 3rd March 2011.

The Council has incorporated the changes from the revised CIPFA Code of Practice into its treasury policies, procedures and practices.

10. Gross and Net Debt:

10.1 The purpose of this treasury indicator is to highlight a situation where the Council is planning to borrow in advance of need.

Upper Limit on Net Debt compared to Gross Debt	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Outstanding Borrowing (at nominal value)	113.87	112.61	113.49	116.50
Other Long-term Liabilities (at nominal value)	0.47	0.23	0.04	0.01
Gross Debt	**114.34**	**112.84**	**113.53**	**116.51**
Less: Investments	**(63.14)**	**(58.88)**	**(57.65)**	**(57.13)**
Net Debt	**51.20**	**53.96**	**55.88**	**59.38**

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

11.1 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 sums outstanding (i.e. fixed rate borrowing less fixed rate investments / fixed rate borrowing).

11.2 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.

	Existing level at 31/03/11 %	2011/12 Approved %	2011/12 Revised %	2012/13 Estimate %	2013/14 Estimate %	2014/15 Estimate %
Upper Limit for Fixed Interest Rate Exposure	42.6%	100%	100%	100%	100%	100%
Upper Limit for Variable Interest Rate Exposure	0%	50%	50%	50%	50%	50%

11.3 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.

12. Maturity Structure of Fixed Rate borrowing:

12.1 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.

12.2 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.

Maturity structure of fixed rate borrowing	Existing level at 31/03/11 %	Lower Limit for 2012/13 %	Upper Limit for 2012/13 %
under 12 months	4.03%	0%	25%
12 months and within 24 months	14.71%	0%	25%
24 months and within 5 years	1.78%	0%	50%
5 years and within 10 years	6.22%	0%	75%
10 years and within 20 years	17.33%	0%	100%
20 years and within 30 years	31.02%	0%	100%
30 years and within 40 years	1.86%	0%	100%
40 years and above	23.05%	0%	100%

13. Credit Risk:

13.1 The Council considers security, liquidity and yield, in that order, when making investment decisions.

13.2 Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the Council's assessment of counterparty credit risk.

13.3 The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution (minimum A- or equivalent) and its sovereign (minimum AA+ or equivalent for non-UK sovereigns);
- Sovereign support mechanisms;
- Credit default swaps (where quoted);
- Share prices (where available);
- Economic fundamentals, such as a country's net debt as a percentage of its GDP);
- Corporate developments, news, articles, markets sentiment and momentum;
- Subjective overlay.

13.4 The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

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

14.1 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.

Upper Limit for total principal sums invested over 364 days	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Estimate £m**	**2013/14 Estimate £m**	**2014/15 Estimate £m**
	40.00	40.00	40.00	40.00	40.00

GWYNEDD COUNCIL'S LIST OF AUTHORISED COUNTERPARTIES

Country	Counterparty	Maximum Limit of Investments £m	Maximum Length of Loans
UK	DMADF, DMO	No Limit	No Limit
UK	UK Local Authorities	£25m (£25m)	1 year
UK	**Santander UK Plc (Banco Santander Group)**	£20m (£20m)	**1 year** (2years)
UK	**Bank of Scotland (Lloyds Banking Group)**	£20m (£20m)	**1 year** (2years)
UK	**Lloyds TSB (Lloyds Banking Group)**	£20m (£20m)	**1 year** (2years)
UK	**Barclays Bank Plc**	£20m (£20m)	**1 year** (2years)
UK	**Clydesdale Bank (National Australia Bank Group)**	£20m (£20m)	**1 year** (2years)
UK	**HSBC Bank Plc**	£20m (£20m)	**1 year** (2years)
UK	**Nationwide Building Society**	£20m (£20m)	**1 year** (2years)
UK	**NatWest (RBS Group)**	£20m (£20m)	**1 year** (2years)
UK	**Royal Bank of Scotland (RBS Group)**	£20m (£20m)	**1 year** (2years)
UK	**Standard Chartered Bank**	£20m (£20m)	**1 year** (2years)
Australia	Australia and NZ Banking Group	£5m (£5m)	1 year
Australia	Commonwealth Bank of Australia	£5m (£5m)	1 year
Australia	National Australia Bank Ltd (National Australia Bank Group)	£5m (£5m)	1 year
Australia	Westpac Banking Corp	£5m (£5m)	1 year
Canada	Bank of Montreal	£5m (£5m)	1 year
Canada	Bank of Nova Scotia	£5m (£5m)	1 year
Canada	Canadian Imperial Bank of Commerce	£5m (£5m)	1 year
Canada	Royal Bank of Canada	£5m (£5m)	1 year
Canada	Toronto-Dominion Bank	£5m (£5m)	1 year
Finland	Nordea Bank Finland	£5m (£5m)	1 year
France	BNP Paribas	£5m (£5m)	1 year
France	Credit Agricole CIB (Credit Agricole Group)	£5m (£5m)	1 year
France	Credit Agricole SA (Credit Agricole Group)	£5m (£5m)	1 year
France	Société Générale	£5m (£5m)	1 year
Germany	Deutsche Bank AG	£5m (£5m)	1 year
Netherlands	ING Bank NV	£5m (£5m)	1 year
Netherlands	Rabobank	£5m (£5m)	1 year
Netherlands	Bank Nederlandse Gemeenten	£5m (£5m)	1 year
Sweden	Svenska Handelsbanken	£5m (£5m)	1 year
Switzerland	Credit Suisse	£5m (£5m)	1 year
US	JP Morgan	£5m (£5m)	1 year

1. There is a limit of £20m on banks within the same banking group.
2. Investments in Non-UK banks will be restricted to a maximum limit of 40% of the portfolio, with a £10m country limit to a maximum of 30% of the portfolio per country.

Please note this list could change if, for example, a counterparty/country is upgraded, and meets our other creditworthiness tools. Alternatively, if a counterparty is downgraded, this list may be shortened.

Instrument	Country	Counterparty	Maximum Limit of Investments £m	Maximum Length of Loans
Gilts*	UK	DMO	No limit	6 years
AAA rated Money Market Funds	UK/Ireland/ Luxembourg	Money Market Funds	£5m per name	Daily Liquidity
Other MMFs and CIS	UK	Collective Investment schemes	£5m per name	Daily Liquidity
Treasury bills*	UK	DMO	No limit	1 year
Local Authority bills*	UK	UK Local Authorities	£25m	1 year
Bonds issued by multilateral development banks.*	Europe/ America	EIB, Council of Europe, Inter American Investment Bank	£5m	6 years
Bonds issued by financial institutions guaranteed by the UK government.*	UK	Guaranteed financial institutions	£5m	6 years
Sterling denominated bonds by non-UK sovereign governments.*	Non-UK	Non-UK Sovereign Governments	£5m	3 years
Business loans to local companies **	UK	As agreed by the Local Loans Fund scheme.	£1m	10 years

* Investment in these instruments will be on advice from the Council's treasury advisor.

** Advancement of these loans will be approved by the procedure detailed in Appendix B, Paragraph 7. Evaluation of the Business Loans is not part of the advice or services from the Council's treasury advisor.