Part I
Release to Press

Stevenage BOROUGH COUNCIL

Meeting:	**COUNCIL**	Agenda Item: **12**
Portfolio Area:	Resources	
Date:	**25 February 2009**	

PRUDENTIAL CODE INDICATORS AND TREASURY MANAGEMENT STRATEGY
(Accountancy)

NON-KEY DECISION

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1 PURPOSE

To recommend to Council, the approval of the 2009/10 Prudential Indicators and Treasury Management Strategy and the proposed changes to the investment limits and terms.

2 RECOMMENDATIONS

2.1 That the Executive proposes to Council the adoption of the Prudential Code Indicators as detailed in Appendix A and the changes to the investment limits proposed in 4.2.8.

2.2 That the Executive proposes to Council the adoption of the 2009/10 Treasury Management Strategy as detailed in paragraph 4.2.

3 BACKGROUND

3.1 The Local Government Act 2003 required that from April 2004 Councils must 'have regard to' the Prudential Code and set Prudential Indicators to ensure that capital investment plans are affordable, prudent and sustainable. The Council has adopted the CIPFA Code of Practice on Treasury Management. These were adopted on 18 May 2004 by the Council. The indicators cover the current year and the next three years.

3.2 The 2003 Act requires the Council to set out its Treasury Strategy for borrowing and to prepare an Annual Investment Strategy; which sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

3.3 It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that arise as a result of capital financing decisions. This therefore means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue are limited to a level which is affordable within the projected income of the Council for the foreseeable future.

3.4 The legislation abolished Credit Approvals, which had previously controlled Council borrowing, in favour of a system in which Affordable Borrowing Limits are determined with regard to the code of practice published by CIPFA 'The Prudential Code for Capital Finance in Local Authorities'.

3.5 In July 2006 the Council submitted a Round Six Arms Length Management Organisation (ALMO) Bid to the Department for Communities and Local Government (DCLG) for some £55million of funding, in the form of ALMO Borrowing, to assist in achieving the Decent Homes target in the Council's HRA Housing Stock. The ALMO Borrowing approval will allow the Council to borrow funds to undertake the Decent Homes works, with the interest charges on the borrowing being funded through the HRA Subsidy System. Access to the ALMO borrowing is dependant upon Stevenage Homes Limited (SHL) achieving at least a Two Star inspection rating when inspected in February 2009.

3.6 The Council has not budgeted for any any long term borrowing during 2009/10 for non-HRA purposes. The Indicators in this report do not therefore, at this stage, take into account the potential ALMO borrowing that may occur in early 2009/10 and it is proposed that a major review of the indicators, investment and borrowing strategy will be undertaken later in the year and brought back for updated approval closer to the timing of accessing the ALMO Borrowing following achievement of the Two Star ALMO rating.

3.7 The Council has experienced difficulties with its land sales disposal programme (as contained within the capital strategy) as a result of the current economic climate. In the December Capital Strategy update, a reduction in capital receipts of £6.14million was identified for 2008/09 and 2009/10. As a result, Members agreed to defer £6.5million from the capital programme. If this trend continues and the Council is unable to realise the sales estimated for 2009/10, then the Council may need to borrow in the future, this scenario is not currently within the five year Capital Strategy. A General Fund budget provision would be required to service debt costs.

4 REASONS FOR RECOMMENDED COURSE OF ACTION AND OTHER OPTIONS

4.1 Prudential Code

4.1.1 A schedule of Prudential Code Indicators with explanatory notes is attached at Appendix A. Those indicators to which regard should be given when determining the Council's treasury management strategy for the next three financial years are denoted by an asterix(*).

4.1.2 The Prudential Code introduced new requirements for the manner in which capital spending plans are to be considered and approved and in conjunction with this, the development of an integrated treasury management strategy. Appendix B details the objectives of the Prudential Code.

4.2 Treasury Management Strategy

4.2.1 Borrowing Strategy-The Operational and Authorised Borrowing Limits have to be approved before the start of each financial year.

4.2.2 As the Council has had debt free status since March 2001, only short term borrowing for cash flow management purposes is currently undertaken and, therefore, the overall and short term limits are identical. In addition, the variable interest proportion is set at 100% - short-term borrowing is likely to be minimal - at variable or fixed rate depending on the availability of funds in the money market.

4.2.3 The limits proposed for 2009/10 (unchanged from 2008/09) are:-

- Overall Borrowing Limit - £15million
- Short Term Borrowing Limit - £15million
- Variable Interest Proportion Limit - 100%

4.2.4 As stated above in paragraphs 3.5 and 3.6, the Council does not anticipate undertaking any long term borrowing during 2009/10 for non-HRA purposes. The Indicators in this report do not, at this stage, take into account the potential ALMO borrowing It is proposed that a major review of the investment and borrowing strategy will be undertaken later in the year and brought back for updated approval closer to the timing of accessing the ALMO Borrowing following achieving the Two Star ALMO rating.

4.2.5 **Prospect for Interest Rates-**The base rate at the start of the financial year was 5.25%, reducing to 5.00% on 10 April, this remained in place until October when rates were cut to 4.5% followed by a 1.5% cut in November to 3% and to 2% in December. In January the Bank of England reduced interest rates to 1.5%, the lowest level since the Bank of England's formation in 1694. The market predicts that interest rates will fall to 0.5% and will remain at that level until 2010 when they should start to gently rise, reaching 4% in 2012. Investment rates on 23 January 2009 are as below.

One month	**1.50%**
Three months	**1.80%**
Six months	**2.15%**
One Year	**2.35%**

The Council has budgeted in 2009/10 an average return on investments of 2.41%. However, due to the current economic climate it may be necessary to review this figure. The Council had ' callable investments ' to the value of £7million which had an average return of 5.72% per annum. One investment has already been 'called' by the borrower and repaid and the remaining two are expected to be repaid on the next 'call' dates in February and May 2009   This has been factored into the forecast return, and it is estimated that the new investments will be at lower rates, typically 2%.

4.2.6 **Investment Strategy-**The Council is required to prepare an Annual Investment Strategy, which sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

4.2.7 In the current economic climate, security of the Council's investments is of major concern. This must be weighed with the fact that investment returns form a significant part of the Council's income.

4.2.8 On 17 November 2009 a report was taken taken to the Special Audit Committee and subsequently passed up to Council changing the existing strategy.   This was in response to the collapse of the Icelandic banks. The Council did not have any money with Icelandic Banks, but it was felt prudent to review the strategy. As a result;

- The lending limits were reduced to £5million per group.
- The exception being the 'call accounts' which kept their limit of £7.5million as these are liquid accounts.

There is now a preference to invest with UK banks which have the backing of the British Government, Appendix E, and it is getting progressively more difficult to find names which meet the stringent criteria in place. In order to allow flexibility in the Council's portfolio of investments, it may be prudent to spread investments over a one to five year period. Therefore it is proposed that;

- the lending limit is returned to £7.5million per group.
- Investments can be dealt for up to five years with the Strategic Director (Resources) approval and limited to those institutions which appears on the Debt Management Office (DMO) web site, Appendix E

4.2.9 The principal consideration when undertaking an investment is the Council's cash flow requirements, i.e.. investments are scheduled to mature on a date when it is known large cash flows will occur. When surplus cash becomes available for investment, it is used to maintain a balanced investment portfolio. As at the end December 2008 the total investments were £36.90million. Average return to date on all investments this year being 5.74**%,** due to the large reduction in base rate and the 'callable deposits' being repaid, the return for the year is likely to be nearer 5.36%.

4.2.10 The Council uses the Sector creditworthiness service. This provides a monthly updated list based on Fitch and Moody ratings, plus updates as they occur. If a downgrade results in the counterparty not meeting the Council's minimum criteria, it will no longer be used for new investments.

4.2.11 A list of banks and building societies, which currently meet our credit worthiness, is attached at Appendix C. A list of the types of instruments comprising Specified and Non-Specified Investments is attached at Appendix D.

4.2.12 The Council currently has £36.49million on deposit with the following institutions

Institution	Amount £'000s
Nationwide BS	3,000
Bank of Scotland	5,000
Bank of Ireland	5,100
CIC Group	2,800
Alliance and Leicester	2,790
Handelsbanken	5,500
Barclays	7,300
Clydesdale	3,000
Abbey	2,000
Total	**36,490**

4.2.13 **Summary - Treasury Management Strategy**

a. That the Prudential Indicators are adopted and kept under review.
b. That surplus funds are invested according to Treasury Policy.
c. That a review will be undertaken in advance of any ALMO borrowing.

5 IMPLICATIONS

5.1 Financial Implications

The report is of a financial nature and outlines the Prudential Code Indicators and the principals under which the Treasury Management functions are managed.

5.2 Legal Implications

Approval of the Prudential Code Indicators and the Treasury Management are intended to ensure that the Council complies with relevant legislation and best practice.

5.3 Policy Implications

The proposed limits are in line with current policy.

BACKGROUND DOCUMENTS

- Statutory Instrument 2003 No 3146 The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003
- CIPFA Prudential Code for Capital Finance in Local Authorities
- Sector Treasury Management Documents

APPENDICES

- Appendix A - Prudential Code Indicators
- Appendix B – Prudential Code Objectives
- Appendix C - Lending List
- Appendix D - Specified and Non-Specified Investments

- Appendix E - Banks Supported by the British Government