Agenda Item 13

Report to: **Audit, Best Value and Community Services Scrutiny Committee**

Date: **5 November 2013**

By: **Chief Operating Officer**

Title of report: **Treasury Management – Half year review for 2013/14.**

Purpose of report: **To present a mid year review of the County Council's performance on treasury management for the half year to 30th September 2013.**

RECOMMENDATIONS: The Audit, Best Value and Community Services Scrutiny Committee is asked to

(1) note our Treasury Management performance for the first six months for 2013/14; and

(2) support the planned review of the treasury management strategy.

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1. Financial Appraisal

1.1 The Code of Practice for Treasury Management requires the review of the Council's treasury management performance to be reported half way through the year as well as at the end of each year.

2. Supporting Information

Introduction

2.1 The County Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance. The County Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Capita and operates its treasury management service in compliance with this Code. These require that the prime objective of the treasury management activity is the effective management of risk, and that its borrowing activities are undertaken in a prudent, affordable and sustainable basis and its treasury management practices demonstrate a low risk approach. The Code requires the regular reporting of treasury management activities to:

- Forecast the likely activity for the forthcoming year (in the Annual Treasury Strategy Report);
- Review actual activity for the proceeding year (in the Annual Stewardship Report);
- Review actual activity mid year (this report); and
- Report changes to our Strategy (when required).

2.2 This report sets out:

- A summary of the original strategy agreed for 2013/14 and the economic factors affecting this strategy in the first six months of this year (Appendix A)
- The treasury management activity during the first six months (Appendix B);
- The performance to date of the Prudential Indicators and compliance within limits (Appendix C).

2.3 The report will be reported to Cabinet for approval on 12 November 2013.

The economic conditions compared to our original strategy for 2013/14

2.4 The original strategy and the economic conditions prevailing in 2013/14 are set out in Appendix A which is attached to this report. 2013/14 has continued the uncertain environment, with more concerns over the economies of other European countries and the UK economy. The main implications have been on-going counterparty risk and low investment returns.

2.5 There is a plan in place to conduct a treasury management strategy review to investigate options to improve returns from investments and understand how those options would affect our risk profile. Any changes to the strategy would have to be approved by the Council who the responsibility to approve the Treasury Management strategy annually.

The treasury activity during the first six months on short term investments and borrowing;

The Treasury Management Strategy

2.6 The strategy for 2013/14, agreed in January 2013, continued the prudent approach and ensured that all investments were only to the highest quality rated banks and only up to a period of one year. A more prudent approach than was set out in the strategy has been adopted because of the uncertainties in the market. Investments in banks were overnight only and were able to be called without notice.

Short term lending

2.7 The total amount received in short term interest for the six months to 30th September 2013 was £0.686m at an average rate of 0.38%. This fell short of the aim to secure investment income of at least base rate on the Council's general cash balances. This against a backdrop of ensuring, so far as possible in the current financial climate, the security of principal and the minimisation of risk. This Council has continued to follow an extremely prudent approach with security and liquidity as the main criteria before yield.

Long term borrowing

2.8 Details of our long term borrowing are included in Appendix B of the report. The important points are:

- No new borrowing was undertaken through PWLB in the first six months and is unlikely in the rest of the year. It was agreed to continue to use "internal borrowing" to finance new capital investment
- Although a proactive approach has been taken to repayment and restructuring of debt, no cost effective opportunities have arisen in the first six months of this year.

Short term borrowing

2.9 No borrowing has been undertaken on a short-term basis so far in 2013/14 to cover temporary overdraft situations.

Prudential Indicators and compliance with limits

2.10 The County Council is required by the Prudential Code to report the actual prudential indicators after the end of each year. These indicators are set out in Appendix C with a comparison of the actual position for the County Council for 2013/14 so far this year.

3. Conclusion and reason for recommendations

3.1 This report updates the Committee and fulfils the requirement to submit a half yearly report in the form prescribed in the Treasury Management Code of Practice. Short term lending in the first 6 months has achieved returns less than base rate. This reflects the target which is to ensure so far as possible in the financial climate, the security of principal and the minimisation of risk. This Council has continued to follow an extremely prudent approach with security and liquidity as the main criteria before yield. Exposure to future risk continues to be minimised through proactive and constant review of the treasury management policy. The emphasis must continue to be able to react quickly if market conditions worsen.

KEVIN FOSTER
Chief Operating Officer

Contact Officers: Marion Kelly , Chief Finance Officer Tel : 01273 335078
Ola Owolabi, Head of Accounts and Pensions. Tel No. 01273 482017
Richard Carcas, Principal Finance Officer, Tel No. 01273 481926

BACKGROUND DOCUMENTS

CIPFA Prudential Code
CIPFA Treasury Management in the Public Services- Code of practice
Local Government Act 2003 Local Government Investments –Guidance from the former Office of the Deputy Prime Minister

Appendix A

A summary of the strategy agreed for 2013/14 and the economic factors affecting this strategy and amendments to the strategy

1. Background information

1.1 Cabinet receive an annual Treasury Management Strategy report in January, which sets out the proposed strategy for the year ahead. This strategy includes the limits and criteria for organisations to be used for the investment of cash surpluses and has to be approved by the County Council.

1.2 This Council has always adopted a prudent approach on its investment strategy and in the last few years, there have been regular changes to the list of the approved organisations used for investment of short term surpluses. This list is regularly reviewed to ensure that the Council is able to invest in the best available rates consistent with low risk; the organisations are regularly monitored to ensure that their financial strength and low risk has been maintained.

1.3 When the original strategy for 2013/14 was drawn up earlier in the year, the money markets were volatile and in this climate ensuring the security of investments continued to be difficult and extreme caution has to be taken on where surplus funds can be invested.

2. Strategy for 2013/14

Borrowing

2.1 County Council's past strategy was to borrow externally to support the Capital Programme and the Council's cash (rather than using internal borrowing). Historically this meant that the interest rate earned on cash balances was higher than the interest rate paid on loans from the Public Works Loans Board (PWLB). In the current financial climate, this interest rate differential has been removed. No new PWLB borrowing has taken place since January 2008 and is unlikely in the current climate unless long term PWLB rates reach a very low level (where the long term benefit would exceed the short term costs). The average rate of all debt at 30 September 2013 of £264.2m is 5.20% and will remain at the same level in 2013/14 if no new loans are taken and no beneficial rescheduling of debt is available.

2.2 Our opportunity to restructure our debt has been significantly reduced since October 2010 as a result of the PWLB increasing all of its lending rates by 1% as part of the Government's Comprehensive Spending Review. However, it did not increase the rate of interest used for repaying debt so that not only the cost of our future borrowing has increased but our opportunity to restructure our debt when market conditions allow has been significantly reduced.

Investment

2.3 When the strategy was agreed in January of this year, the advice given to us by our advisors, Capita, was that short term rates were expected to remain on hold for a considerable time. Economic forecasting remained troublesome with so many extermal influences weighing on the UK. There was consensus among analysts that the economy would remain weak and key areas of uncertainty included:

- a worsening of the Eurozone debt crisis and heightened risk of the breakdown of the bloc or even of the currency itself; the impact of the Eurozone crisis on financial markets and the banking sector;
- the impact of the Government's austerity plan on confidence and growth and the need to rebalance the economy from services to exporting manufactured goods;
- the under-performance of the UK economy which could undermine the Government's policies that have been based upon levels of growth that inceasingly seem likely to be undershot;
- a continuation of high levels of inflation ;
- the economic performance of the UK's trading partners, in particular the EU and US, with some analysts suggesting that recession could return to both;
- stimulus packages failing to stimulate growth; potential for protectionism i.e. an escalation of the currency war / trade dispute between the US and China.

2.4 The overall balance of risks remained weighted to the downside. Lack of economic growth, both domestically and overseas, would impact on confidence putting upward pressure on unemployment. It would also further knock levels of demand which would bring the threat of recession back into focus.

2.5 Capita believed that the longer run trend is for gilt yields and PWLB rates to rise due to the high volume of gilt issuance in the UK, and the high volume of debt issuance in other major western countries.

2.6 Given the weak outlook for economic growth, Capita saw the prospects for any interest rate changes before mid-2013 as very limited. There was potential for the start of Bank Rate increases to be even further delayed if growth disappointed.

3. Investment Strategy agreed for 2013/14

3.1 The strategy ensured that in the current economic climate a prudent approach was maintained. This would be achieved through investing with selected banks and funds which meet the Council's rating criteria. The emphasis would continue on security (protection of the capital sum invested) and liquidity (keeping money readily available for expenditure when needed) rather than yield. The strategy continued with this prudent approach and no change was proposed to change the agreed strategy for 2013/14.

3.2 It was recognised that movements within the money markets can happen with no notice and the Chief Finance Officer would have to amend this strategy in order to safeguard Council funds. As in the past any such actions would be reported to the next Cabinet meeting.

3.3 It was not anticipated that any new external borrowing would be undertaken in 2013/14, however the limits set out in the Authorised Limit for Borrowing would allow such borrowing if market conditions change. External borrowing would only take place if the rates available were so low that the long term benefits would significantly exceed the short term cost.

3.4 Opportunities for cost effective repayment of existing debt and restructuring opportunities were to be constantly monitored and would be taken if and when they emerge.

3.5 The County Council funds can be invested as follows:-

(A) UK Investment Without Government Equity Holding

Up to a maximum of £60m deposited up to a period of up to one year with any of the following: -

The current policy stance was overnight but the policy allowed changes to reflect market conditions if and when they improved.

Bank / Fund / Local Authority
Barclays
Santander UK
HSBC
Nationwide
Individual Treasury Type Money Market Funds (AAA rated) which invest in Government Securities only
Individual Cash Type Money Market Funds (AAA rated)
Another Local Authority (Equivalent to the low risk of investing with the Government but not formally rated)

Only banks which met the following minimum rating criteria for at least two of the designated agencies to be used.

Ratings Agency	Long Term	Short Term
Fitch	AA-	F1+
Moody	AA3	P-1
Standards and Poors	AA-	A-1+

(B) UK Investment With Government Equity Holding of minimum of 30%

30% was agreed as a minimum level of significant associated company influence. In practice it serves as a trigger to formally review our position.

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Up to a maximum of £60m deposited up to a period of up to three months with the following: -

The policy stance was overnight but the policy allowed changes to reflect market conditions if and when they improved.

Bank
Lloyds/HBOS Nat West/RBS

Only banks which met the following minimum rating criteria for at least two of the designated agencies were to be used. The banks would not be used if the UK Sovereign rating falls below AAA.

Ratings Agency	Long Term	Short Term
Fitch	A	F1
Moody	A2	P-1
Standards and Poors	A	A-1

The policy retained the ability to revert to some, or even extensive use of the Government's Debt Management Account Deposit Facility (DMADF) if market risk conditions tightened. Other very safe alternative investments would be explored if they become available.

It was continued to be recognised that movements within the money markets can happen with no notice and the Chief Finance Officer would have to amend this strategy in order to safeguard Council funds. As in the past any such actions would be reported to the next Cabinet meeting.

3.6 The strategy going forward continued with the policy of ensuring minimum risk but will also need to deliver secure investment income of at least bank rate on the Council's cash balances. (The actual target is bank rate). The reduction to bank rate for 2013/14 reflected the lower rates available in the market on the change to more prudent investments.

3.7 Additional requirements under the Code of Practice require the Council to supplement credit rating information. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information has been and will continue to be applied before making any specific investment decision from the agreed pool of counterparties. This additional market information (for example Sovereign ratings, Credit Default Swaps, equity prices, the Capita security and liquidity model and the CIPFA National treasury risk model as well as media updates etc.) is assessed when comparing the relative security of differing investment counterparties.

3.8 All Money Market Funds used would be monitored and chosen by the size of fund, rating agency recommendation, exposure to other Countries (Sovereign debt), weighted average maturity and weighted average life of fund investment and counterparty quality.

3.9 All of the investments were classified as Specified Investments. These investments were sterling investments of not more than one-year maturity with institutions deemed to be high credit quality or with the UK Government (Debt Management Account Deposit Facility). These were considered low risk assets where the possibility of loss of principal or investment income was small. The County Council does not have any Non Specified Investments which are more than one-year maturity or with institutions which have a lesser credit quality.

4. Economic factors affecting the Strategy in 2013/14 (commentary supplied by our advisors Capita).

The first six months of 2013/14

4.1 During 2013/14 economic indicators suggested that the economy is recovering, albeit from a low level. After avoiding recession in the first quarter of 2013, with a 0.3% quarterly expansion the economy grew 0.7% in Q2. There have been signs of renewed vigour in household spending in the summer, with a further pick-up in retail sales, mortgages, house prices and new car registrations.

4.2 The strengthening in economic growth appears to have supported the labour market, with employment rising at a modest pace and strong enough to reduce the level of unemployment further. The Bank of England extended its Funding for Lending Scheme (FLS) into 2015 and sharpened the incentives for banks to extend more business funding, particularly to small and medium size enterprises. To date, the mortgage market still appears to have been the biggest beneficiary from the scheme, with mortgage interest rates falling further to new lows. Together with the Government's Help to Buy scheme, which provides equity loans to credit-constrained borrowers, this is helping to boost demand in the housing market. Mortgage approvals by high street banks have risen as have house prices, although they are still well down from the boom years pre 2008.

4.3 Turning to the fiscal situation, the public borrowing figures continued to be distorted by a number of one-off factors. On an underlying basis, borrowing in Q2 started to come down, but only slowly, as Government expenditure cuts took effect and economic growth started to show through in a small increase in tax receipts. The 2013 Spending Review, covering only 2015/16, made no changes to the headline Government spending plan, and monetary policy was unchanged

4.4 Bank Rate is unlikely to change until unemployment first falls to 7%, which was not expected until mid 2016. However, 7% is only a point at which the MPC will review Bank Rate, not necessarily take action to change it. The three month to July average rate was 7.7%.

4.5 Tensions in the Eurozone eased over the second quarter, but there remained a number of triggers for a renewed flare-up. Economic survey data improved consistently over the first half of the year, pointing to a return to growth in Q2, so ending six quarters of Eurozone recession.

Outlook for the rest of 2013/14

4.6 Economic forecasting remains difficult with so many external influences weighing on the UK. Volatility in bond yields is likely during 2013/14 as investor fears and confidence ebb and flow between favouring more risky assets i.e. equities, and safer bonds. Downside risks to UK gilt yields and PWLB rates include:

- A return to weak economic growth in the US, UK and China causing major disappointment to investor and market expectations
- The potential for a significant increase in negative reactions of populaces in Eurozone countries against austerity programmes, especially in countries with very high unemployment rates e.g. Greece and Spain, which face huge challenges in engineering economic growth to correct their budget deficits on a sustainable basis.
- Problems in Eurozone heavily indebted countries (e.g. Cyprus and Portugal) which could also generate safe haven flows into UK gilts.
- Monetary policy action failing to stimulate sustainable growth in western economies, especially the Eurozone and Japan.
- Weak growth or recession in the UK's main trading partners - the EU and US, depressing economic recovery in the UK.
- Geopolitical risks e.g. Syria, Iran, North Korea, which could trigger safe haven flows back into bonds

Upside risks to UK gilt yields and PWLB rates, especially for longer term PWLB rates include: -

- UK inflation being significantly higher than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

- Increased investor confidence that sustainable robust world economic growth is firmly expected, together with a reduction or end of QE operations in the US, causing a further flow of funds out of bonds into equities.
- A reversal of Sterling's safe-haven status on a sustainable improvement in financial stresses in the Eurozone.
- In the longer term - a reversal of QE in the UK; this could initially be implemented by allowing gilts held by the Bank to mature without reinvesting in new purchases, followed later by outright sale of gilts currently held.
- Further downgrading by credit rating agencies of the creditworthiness and credit rating of UK Government debt, consequent upon repeated failure to achieve fiscal correction targets and sustained recovery of economic growth, causing the ratio of total Government debt to GDP to rise to levels that provoke major concern.

The overall balance of risks to economic recovery in the UK is now weighted to the upside after five months of robust good news on the economy. However, only time will tell just how long this period of strong economic growth will last, and it remains exposed to vulnerabilities in a number of key areas. The longer run trend is for gilt yields and PWLB rates to rise, due to the high volume of gilt issuance in the UK, and of bond issuance in other major western countries

Appendix B

The treasury management activity during the first half year

1. Short term lending interest rates

1.1 Base interest rate has stayed at 0.5% in 2013/14 to date. The rate is the lowest ever and has remained unchanged for the longest period on record. The last change was on 5th March 2009.

1.2 There have been continued uncertainties in the markets during the year to date as set out in Section 4 of Appendix A.

1.3 Additional market information including Sovereign ratings, Credit Default Swaps, equity prices, the Capita security and liquidity model and the CIPFA National treasury risk model as well as media updates etc have been used to assess the relative security of differing investment counterparties.

1.4 The strategy for 2013/14, agreed in January 2013, continued the prudent approach and ensured that all investments were only to the highest quality rated banks and only up to a period of one year. No changes to this Strategy have been required but a more prudent approach has been adopted because of the uncertainties in the market. Investments in all banks continued to be on call (overnight only).

1.5 The total amount received in short term interest for the six months to 30th September 2013 was £0.686m at an average rate of 0.38%. This was below the average of base rates in the same period (0.5%) and fell short of the aim to secure investment income of at least base rate on the Council's general cash balances. This is against a backdrop ensuring, so far as possible in the financial climate, the security of principal and the minimisation of risk.

1.6 The interest rate received on all MMFs has reduced during the first six months and the "Treasury Type" MMFs and the Government's Debt Management Account Deposit Facility (DMADF) rates received are less than received on "Cash Type" MMFs. The reason for these changes was the continued major concerns in the market due to the problems with European countries and the Euro and these have been set out in Section 4 of Appendix A. The changes to the investments held comply with our Treasury Management Strategy and this Council has continued to follow an extremely prudent approach with security and liquidity as the main criteria before yield.

2. Long term borrowing

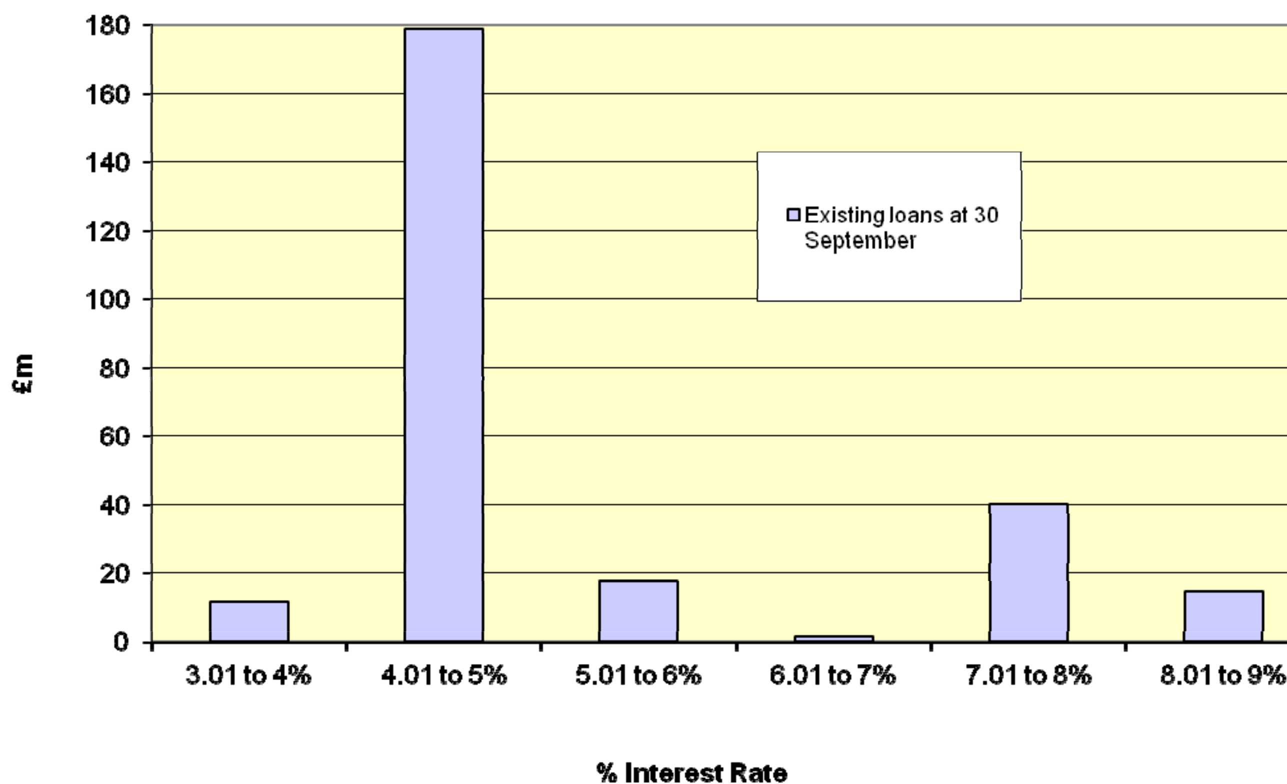
2.1 The County Council has had a strategy to borrow to support the Capital Programme and lend out other cash (rather than using internal borrowing). Historically this meant that the interest rate earned on cash balances was higher than the interest rate paid on loans from the Public Works Loans Board (PWLB). In the current financial climate, this interest rate differential has been removed. The cost of new borrowing is now well in excess of the rate achievable on our investments. No new PWLB borrowing has taken place since January 2008 and is unlikely in the current climate unless long term PWLB rates reach a very low level (where the long term benefit would exceed the short term costs).

2.2 The average interest rate of all debt at 30 September 2013 (£264.2m) was 5.20% and will be unchanged at 31 March 2014 as long as no new loans are taken and no beneficial rescheduling of debt is available.

2.3 Opportunities for cost effective repayment of existing debt and restructuring opportunities were constantly monitored but none emerged in the first six months of the year.

2.4 The Department of Communities and Local Government has asked local authorities to make a return to enable them to benefit from a small reduction in all of the PWLB rates for new loans. The PWLB "certainty rate" as it has been named will reduce PWLB borrowing rates by 0.20% for most local authorities. A return has been submitted to keep our options open but despite this reduction it will be unlikely that East Sussex will be borrowing as the long term benefit will still not exceed the short term costs.

The range of interest rates payable in all of the loans is illustrated in the graph below:



3. Short term borrowing

3.1 No borrowing has been undertaken on a short-term basis during 2013/14 to date to cover temporary overdraft situations.

4 Treasury Management Advisers

4.1 The Strategy for 2013/14 explained that the County Council uses Capita as its treasury management consultant on a range of services which include:

- Technical support on treasury matters, capital finance issues and advice on reporting;
- Economic and interest rate analysis;
- Debt services which includes advice on the timing of borrowing;
- Debt rescheduling advice surrounding the existing portfolio;
- Generic investment advice on interest rates, timing and investment instruments;
- Credit ratings from the three main credit rating agencies and other market information;
- Assistance with training on treasury matters

Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remained with the Council. This service remains subject to regular review.

4.2 Capita is the largest provider of Treasury Management advice services to local authorities in the UK and they claim to be the market-leading treasury management service provider to their clients.

4.3 The advice will continue to be monitored regularly to ensure a continued excellent level of advisory service provided to our authority.

Appendix C

Prudential Indicators and compliance with limits – 2103/14

1.1 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. The prudential indicators and limits for the County Council were agreed by the Cabinet on 29 January 2013 within the Update to the Treasury Management Strategy for 2013/14. Below is a table of Current PI's outlining our compliance.

Prudential Indicator	**Compliant**
Capital Expenditure	Yes
Ratio of Financing Costs to Net Revenue Stream	Yes
Capital Financing Requirement (CFR)	Yes
Net external Borrowing compared to the medium term CFR	Yes
Upper limits for fixed interest rate exposure and variable interest rate exposure	Yes
Upper limit for total principal sums invested over 365 days	Yes
Actual External Debt	Yes
Authorised Limit for External Debt	Yes
Operational Boundary for External Debt	Yes
Maturity Structure of Fixed Rate Borrowing	Yes
Maturity Structure of Investments (paragraph 1.3 below)	Yes
Incremental Impact of Capital Investment Decisions	Yes
Adoption of the CIPFA Treasury Management Code (paragraph 1.4 below)	Yes
Interest rate exposures	Yes
Interest rate on long term borrowing	Yes
Interest on investments (paragraph 1.5 below)	Yes
Capital Financing Requirement and Minimum Revenue Provision (paragraph 1.6 below)	Yes

1.2 **Operational boundary and authorised borrowing limit.**

The tables below sets out the estimate and projected capital financing requirement and long-term borrowing in 2013/14

	CAPITAL FINANCING REQUIREMENT	**2013/14**	**2013/14**
		Estimate £m	**Likely Actual £m**
	Capital financing requirement at 1 April 2012	390*	**387***
ADD	Borrowing to support capital programme	19	20
LESS	Provision for repayments of debt	-13	-16
		-------	-------
	Capital financing requirement at 31 March 2013	**396**	**391**
ADD	Net borrowing for next year	59	

	Operational boundary	**455**	
ADD	Short term borrowing	20	Nil

	Authorised limit	**475**	

* Includes an amount for PFI Schemes and Finance Leases.

	ACTUAL BORROWING	**2013/14**
		Likely Actual £m
	Long term borrowing at 1 April 2013	264.2
	Payback of maturing PWLB loan	(1.3)
	No new borrowing anticipated in 2013/14	-

	Long term borrowing at 31 March 2014	262.9

The Operational boundary for borrowing was based on the same estimates as the authorised limit. It reflected directly the authorised borrowing limit estimate without the additional amount for short term borrowing included to allow, for example, for unusual cash movements. The Operational boundary represents a key management tool for in year monitoring and long term borrowing control.

The Authorised limit was consistent with the County Council's current commitments, existing plans and the proposals for capital expenditure and financing, and with its approved treasury management policy statement and practices. It was based on the estimate of most likely, prudent but not worst case scenario, with in addition sufficient headroom (short term borrowing) over and above this to allow for day to day operational management, for example unusual cash movements or late receipt of income. Risk analysis and risk management strategies were taken into account as were plans for capital expenditure, estimates of the capital financing requirement and estimates of cash flow requirements for all purposes.

The Authorised limit is the "Affordable Borrowing Limit" required by S3 of the Local Government Act 2003 and must not be breached. The estimated Long term borrowing at 31 March 2013 of £262.9m is under the Operational boundary and Authorised limit set for 2013/14. The Operational boundary and Authorised limit have not been exceeded during the year to date and will not be exceeded in the rest of the year.

1.3 Maturity structure of investments

The Investment Guidance issued by the former Office of the Deputy Prime Minister, allowed local authorities the freedom to invest for more than for one year. All investments over one year were to be classified as Non-Specified Investments. The County Council had taken advantage of this freedom in previous years. No Non-Specified Investments are held within our overall portfolio of investments and in line with our prudent approach in our strategy, no new long term investments (over 364 days) will be taken in 2013/14.

1.4 Compliance with the Treasury Management Code of Practice

East Sussex County Council has adopted the CIPFA *Code of Practice for Treasury Management in the Public Services.*

1.5 Interest on investments

The table below sets out the average monthly rate received on our investments and compares it to the Bank of England Base rate to reflect the interest rates available in the market, the reduced term of the investment to an overnight (on call) policy and limitation in the use of counterparties.

Month	Amount £000	Monthly rate	Margin against Base
April	140.7	0.50%	-
May	129.0	0.41%	(0.09%)
June	103.9	0.34%	(0.16%)
July	108.0	0.34%	(0.16%)
August	103.8	0.33%	(0.17%)
September	101.1	0.34%	(0.16%)
First six months of 2013/14	**686.5**	**0.38%**	**(0.12%)**

The total amount received in short term interest for the six months to 30th September 2013 was £0.686m at an average rate of 0.38%. This was above the average of base rates in the same period (0.5%) but below the aim to secure investment income of at least base rate on the Council's general cash balances whilst ensuring, so far as possible in the financial climate, the security of principal and the minimisation of risk.

1.6 Capital Financing Requirement and Minimum Revenue Provision (MRP)

The Council's Borrowing Need (the Capital Financing Requirement)

The prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of Council's underlying borrowing need.

The Council was asked to approve the CFR projections below:

CFR including appropriate balances and MRP charges for PFI Schemes and Finance Leases.

	2013/14 Likely Actual	2014/15 Estimate	2015/16 Estimate
	£m	**£m**	**£m**
Total CFR	**390**	**395**	**400**
Movement in CFR	4	5	5

Movement in CFR represented by			
Net financing need for the year (above)	20	21	21
MRP/VRP and other financing movements	-16	-16	-16
Movement in CFR	**4**	**5**	**5**

The Council is required to pay off an element of the accumulated General Fund capital spend each year through a revenue charge (the Minimum Revenue Provision – MRP). The Capital Financing Requirement and Minimum Revenue Provision will not be exceeded in 2013/14.

Minimum Revenue Provision (MRP) Statement

1.7 The statutory requirement for local authorities to charge the Revenue Account each year with a specific sum for debt repayment has been replaced with a more flexible statutory guidance. A variety of options is provided to councils to replace the existing Regulations, so long as there is a prudent provision.

1.8 The statutory duty is that a local authority shall determine for the financial year an amount of minimum revenue provision (MRP) that it considers to be prudent. This replaces the previous prescriptive requirement that the minimum sum should be 4% of the Council's Capital Financing Requirement (CFR).

1.9 To support the statutory duty the Government also issued a guidance, which required that a Statement on the Council's policy for its annual MRP should be submitted to the full Council for approval before the start the financial year to which the provision will relate. The Council are therefore legally obliged to have regard to this MRP guidance in the same way as applies to other statutory guidance such as the CIPFA Prudential Code, the CIPFA Treasury Management Code and the CLG guidance on Investments.

1.10 The MRP guidance offered four options under which MRP might be made, with an overriding recommendation that the County Council should make prudent provision to redeem its debt liability over a period which is commensurate with that over which the capital expenditure is estimated to provide benefits (i.e. estimated useful life of the asset being financed).

1.11 The move to International Financial Reporting Standards (IFRS) involved Private Finance Initiative (PFI) contracts and some leases (being reclassified as finance leases instead of operating leases) coming onto the County Council Balance Sheets as long term liabilities. This new accounting treatment impacted on the Capital Financing Requirement with the result that an annual MRP provision will be required.

1.12 The policy recommended for adoption from 1 April 2013 retained the key elements of the policy previously approved but now incorporates the IFRS changes (re PFI and finance leases) and the consequential updated Government Guidance.

The policy for 2013/14 is therefore as follows:-

1.17 For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy has been:

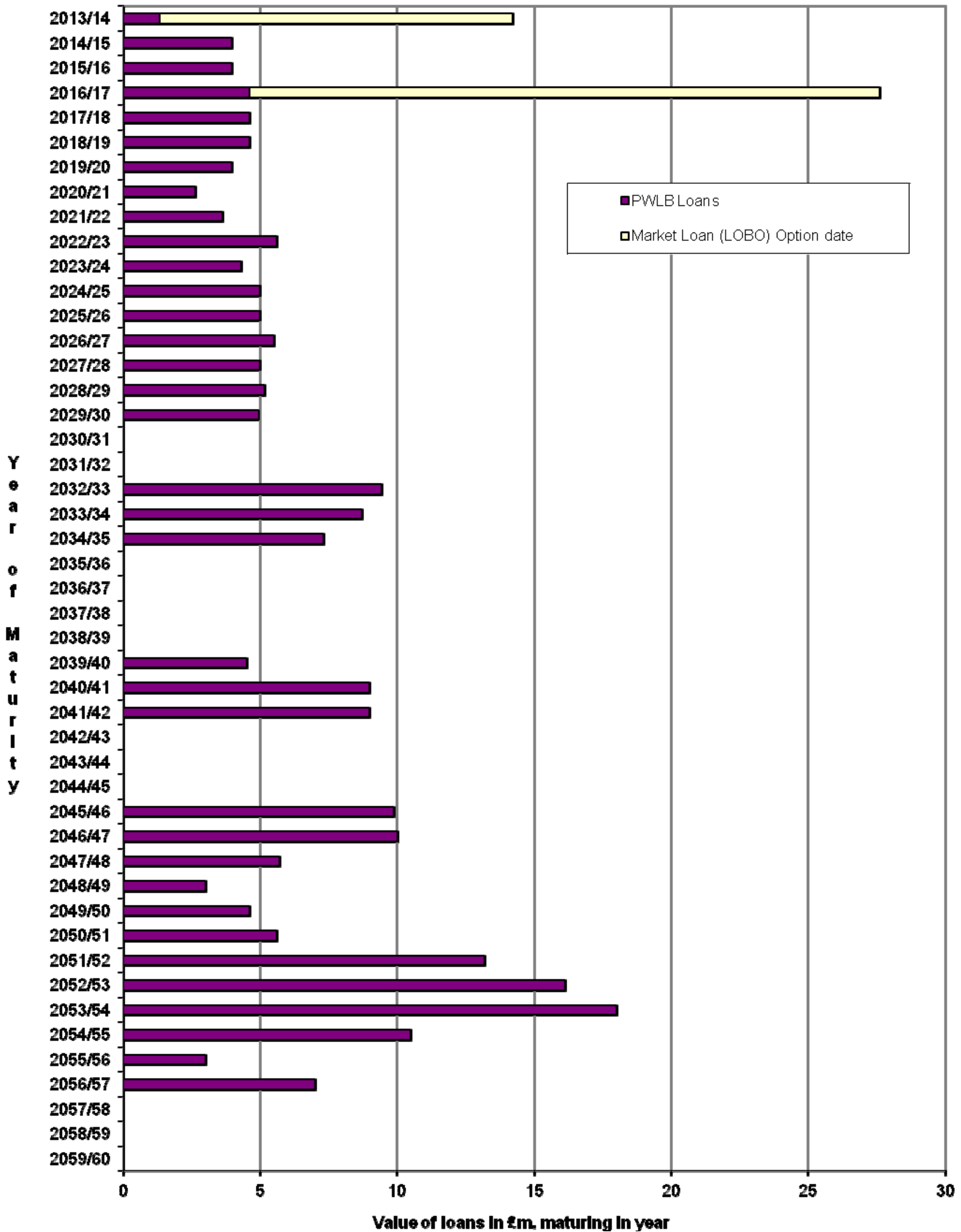
- Based on based on the non-housing CFR, i.e., The Council currently set aside a Minimum Repayment Provision based on basic MRP of 4% each year to pay for past capital expenditure and to reduce its CFR.

1.18 From 1 April 2008 for all unsupported borrowing the MRP policy has been:

- Asset Life Method – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations (this option will be applied for any expenditure capitalised under a Capitalisation Direction).

- Asset Life Method (annuity method) The Council will also be adopting the annuity method, - MRP calculated according to the flow of benefits from the asset, and where the principal repayments increase over the life of the asset. The policy is being adopted as a result of any PFI's assets coming on the balance sheet and any related MRP will be equivalent to the "capital repayment element" of the annual service charge payable to the PFI Operator and for finance leases, MRP will also be equivalent to the "capital repayment (principal) element" of the annual rental payable under the lease agreement.

Under both methods, the Council has the option to charge more than the statutory MRP each year through a Voluntary Revenue Provision (VRP).



Debt Maturity Profile at 30 September 2013
2013/14
2014/15
2015/16
2016/17
2017/18
2018/19
2019/20
2020/21
2021/22
2022/23
2023/24
2024/25
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2051/52
2052/53
2053/54
2054/55
2055/56
2056/57
2057/58
2058/59
2059/60
Year of Maturity
PWLB Loans
Market Loan (LOBO) Option date
0
5
10
15
20
25
30
Value of loans in £m. maturing in year