

## GREATER MANCHESTER INTEGRATED TRANSPORT AUTHORITY

### Report for Resolution

<b>DATE</b>	12 February 2010
<b>REPORT TO</b>	Audit Committee
<b>SUBJECT</b>	Treasury Management Strategy Statement and Borrowing Limits for 2010-11 and Prudential and Treasury Indicators 2010-11 to 2012-13
<b>REPORT OF</b>	Treasurer

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#### **Purpose of the report**

To set out the proposed Treasury Management Strategy Statement and Borrowing Limits for 2010-11 and Prudential and Treasury Indicators for 2010-11 to 2012-13.

#### **Recommendations**

1. The proposed Treasury Management Strategy Statement be approved for submission to the Authority.
2. The Prudential and Treasury Indicators listed in Appendix A be approved for submission to the Authority.
3. The Borrowing Requirements listed in section 5 be approved for submission to the Authority.
4. To note that the Authority will be recommended to amend its constitution in order to adopt the revised Treasury Management Code as set out at Appendix D.

#### **Financial consequences for the revenue budget**

The capital financing charges from estimated borrowing are provided for within the Authority's Revenue Budget, as presented to the meeting of the Authority on 12 February 2010.

#### **Financial consequences for the capital budget**

Amounts that may be borrowed to fund capital expenditure reflect decisions on the levels of capital spending and financing needs. These will be brought for the Authority's approval early in the new financial year.

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#### **Background Documents**

Reports by Sector Treasury Services (Manchester City Council's Treasury Advisors)

Accounting and Financial records are held in rooms 102 and 609.

## 1. Introduction

### 1.1 The Revised CIPFA Treasury Management Code of Practice 2009

In the light of the Icelandic situation in 2008, CIPFA has amended the CIPFA Treasury Management in the Public Services Code of Practice (the Code), Cross-Sectoral Guidance Notes and Guidance Notes and the template for the revised Treasury Management Policy Statement. It is also a requirement of the Code that this Authority should formally adopt the Code. As the Code has been revised, there is a separate appendix to this report where the Authority is asked to adopt the revised Code (Appendix D) and the revised Treasury Management Policy Statement (Appendix C).

The revised Code has emphasised a number of key areas including the following: -

- a) All Authorities must formally adopt the revised Code and four clauses
- b) The strategy report will affirm that the effective management and control of risk are prime objectives of the Authority's treasury management activities.
- c) The Authority's appetite for risk must be clearly identified within the strategy report and will affirm that priority is given to security of capital and liquidity when investing funds and explain how that will be carried out.
- d) Responsibility for risk management and control lies within the organisation and cannot be delegated to any outside organisation.
- e) Credit ratings should only be used as a starting point when considering risk. Use should also be made of market data and information, the quality financial press, information on government support for banks and the credit ratings of that government support.
- f) Authorities need a sound diversification policy with high credit quality counterparties and should consider setting country, sector and group limits.
- g) Borrowing in advance of need is only to be permissible when there is a clear business case for doing so and only for the current capital programme or to finance future debt maturities.
- h) The main annual treasury management reports MUST be approved by full Authority.
- i) There needs to be, at a minimum, a mid year review of treasury management strategy and performance. This is intended to highlight any areas of concern that have arisen since the original strategy was approved.
- j) Each Authority must delegate the role of scrutiny of treasury management strategy and policies to a specific named body.
- k) Treasury management performance and policy setting should be subjected to prior scrutiny.
- l) Members should be provided with access to relevant training.
- m) Those charged with governance are also personally responsible for ensuring they have the necessary skills and training.
- n) Responsibility for these activities must be clearly defined within the organisation.
- o) Officers involved in treasury management must be explicitly required to follow treasury management policies and procedures when making investment and borrowing decisions on behalf of the Authority (this will form part of the updated Treasury Management Practices).

This strategy statement has been prepared in accordance with the revised Code. Accordingly, the Authority's Treasury Management Strategy will be approved annually by the full authority. In addition there will be monitoring reports and regular review by

members in both executive and scrutiny functions. The aim of these reporting arrangements is to ensure that those with ultimate responsibility for the treasury management function appreciate fully the implications of treasury management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

This Authority will adopt the following reporting arrangements in accordance with the requirements of the revised Code: -

<b>Area of Responsibility</b>	<b>Authority/ Committee/ Officer</b>	<b>Frequency</b>
Treasury Management Policy Statement (revised)	Full Authority	Initial adoption in 2010
Treasury Management Strategy / Annual Investment Strategy / MRP policy	Full Authority	Annually before the start of the year
Treasury Management Strategy / Annual Investment Strategy / MRP policy – updates or revisions at other times	Full Authority	As and when necessary
Annual Treasury Outturn Report	Full Authority	Annually by 30 September reporting on activity for the previous financial year.
Treasury Management Monitoring Reports	Audit Committee	Annually by 30 November reporting on activity in the first 6 months.
Scrutiny of treasury management strategy	Audit Committee	Annually before the start of the year
Scrutiny of treasury management performance	Audit Committee	As and when necessary

## **1.2 Revised CIPFA Prudential Code**

CIPFA has also issued a revised Prudential Code which primarily covers borrowing and the Prudential Indicators. Three of these indicators have now been moved from being Prudential Indicators to being Treasury Indicators: -

- authorised limit for external debt
- operational boundary for external debt
- actual external debt.

However, all indicators are to be presented together as one suite. In addition, where there is a significant difference between the net and the gross borrowing position, the risks and benefits associated with this strategy should be clearly stated in the annual strategy.

## **1.3 Revised Investment Guidance**

It should also be noted that the Department of Communities and Local Government is currently undertaking a consultation exercise on draft revised investment guidance which will result in the issue of amended investment guidance for English local authorities to

come into effect from 1 April 2010. It is not currently expected that there will be any major changes required over and above the changes already required by the revised Code.

#### **1.4 Treasury Management Strategy for 2010/11**

The Local Government Act 2003 (the Act) and supporting regulations requires the Authority to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Authority's capital investment plans are affordable, prudent and sustainable.

The Act therefore requires the Authority to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance issued subsequent to the Act) (included as Section 8 of this report); this sets out the Authority's policies for managing its investments and for giving priority to the security and liquidity of those investments.

The suggested strategy for 2010/11 in respect of the following aspects of the treasury management function is based upon the treasury officers' views on interest rates, supplemented with leading market forecasts provided by the Manchester City Council's treasury advisor, Sector Treasury Services.

The strategy covers:

- Section 1. Introduction
  - Section 2. Treasury Limits for 2010/11 to 2012/13
  - Section 3. Prudential and Treasury Indicators for 2010/11 to 2012/13
  - Section 4. Current Portfolio Position
  - Section 5. Borrowing Requirement
  - Section 6. Borrowing Strategy and prospects for Interest rates
  - Section 7. Debt Rescheduling
  - Section 8. Annual Investment Strategy
  - Section 9. MRP Strategy
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- Appendix A List of Prudential and Treasury Indicators for approval
  - Appendix B MRP Strategy
  - Appendix C Treasury Management Policy Statement
  - Appendix D Adoption of Revised CIPFA Treasury Management Code of Practice 2009
  - Appendix E Treasury management scheme of delegation
  - Appendix F The treasury management role of the section 151 officer
  - Appendix G Economic Background
  - Appendix H Prospects for Interest Rates
  - Appendix I Glossary of Terms

## 1.5 Balanced Budget Requirement

It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Authority to produce a balanced budget. In particular, Section 32 requires an Authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This, therefore, means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from: -

- increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
- Any increases in running costs from new capital projects are limited to a level which is affordable within the projected income of the Authority for the foreseeable future.

## 2. Treasury Limits for 2010/11 to 2012/13

- 2.1 There is a statutory duty, under section 3 of the Local Government Act 2003 and supporting regulations, for the Authority to determine and keep under review how much it can afford to borrow. The amount so determined is termed the Authorised Limit.
- 2.2 The Authority must have regard to the Prudential Code when setting the Authorised Limit, which, essentially, requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future levy levels is acceptable.
- 2.3 Whilst termed an "Affordable Borrowing Limit", the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is to be set, on a rolling basis, for the forthcoming financial year and two successive financial years, details of the Authorised Limit can be found in appendix A of this report.

## 3. Prudential and Treasury Indicators for 2010/11 to 2012/13

Prudential and Treasury Indicators (as set out in appendix A to this report) are relevant for the purposes of setting an integrated treasury management strategy.

The Authority is also required to indicate if it has adopted the CIPFA Code of Practice on Treasury Management. This original 2001 Code was adopted on 5<sup>th</sup> December 2003 by the full Authority and the revised Code will be adopted on 23rd April 2010.

## 4. Current Portfolio Position

- 4.1 The Authority's estimated treasury portfolio position at 31 March 2010 will comprise:

	£000	£000	Average Rate
<u>Fixed Rate Funding</u>			
PWLB	182,581		6.41%
Market	60,000		4.22%
		<b>242,581</b>	

<u>Variable Rate Funding</u>		
Market	59,912	4.38%
	<b>59,912</b>	
<b>Gross Debt</b>	<b>302,493</b>	<b>5.57%</b>
Temporary Investments-Market	(90,000)	0.37%
Temporary Investments-Interbank	(5,000)	0.25%
<b>Net Debt</b>	<b>207,493</b>	

## 5. Borrowing Requirement

5.1 The potential long-term borrowing requirements over the next three years, including borrowing for Metrolink and the Transport Delivery Programme, is as follows:-

	<b>2010/11</b>	<b>2011/12</b>	<b>2012/13</b>
	<b>£000</b>	<b>£000</b>	<b>£000</b>
Potential New Long-term borrowing	223,939	325,425	270,688

5.2 It should be noted, however, that cash balances remain strong and new borrowing will normally only be undertaken when it is viewed as optimum for the Authority's longer term financial position even if, in the short term, there is a real cost of 'carrying' the funds as investments.

## 6. Borrowing Strategy and prospects for interest rates

### 6.1 Interest rates

The Authority use Sector Treasury Services who are Manchester City Council's external treasury management advisors, to assist the Authority to formulate a view on interest rates. Appendix H draws together a number of current City forecasts for short term (Bank Rate) and longer fixed interest rates. The following table gives the Sector central view.

#### **Sector Bank Rate forecast for financial year ends (March)**

- **2010 0.50%**
- **2011 1.50%**
- **2012 3.50%**
- **2013 4.50%**

There is downside risk to these forecasts if recovery from the recession proves to be weaker and slower than currently expected. A detailed view of the current economic background is contained within appendix G to this report.

## 6.2 Borrowing rates

The Sector forecast for the PWLB new borrowing rate is as follows: -

	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Mar-12	Mar-13
Bank rate	0.50%	0.50%	0.75%	1.00%	1.50%	3.50%	4.50%
5yr PWLB rate	3.05%	3.20%	3.30%	3.40%	3.60%	4.60%	4.85%
10yr PWLB rate	4.00%	4.05%	4.15%	4.30%	4.45%	5.00%	5.15%
25yr PWLB rate	4.55%	4.65%	4.70%	4.80%	4.90%	5.20%	5.35%
50yr PWLB rate	4.60%	4.70%	4.75%	4.90%	5.00%	5.30%	5.45%

A more detailed Sector forecast is included in appendix H.

In view of the above forecast the Authority's borrowing strategy will be based upon the following information.

- Rates are expected to gradually increase during the year so it should therefore be advantageous to time new long term borrowing for the start of the year when 25 year PWLB rates fall back to or below the central forecast rate of about 4.65%, a suitable trigger point for considering new fixed rate long term borrowing.
- Variable rate borrowing is expected to be cheaper than long term borrowing and will therefore be attractive throughout the financial year compared to taking long term fixed rate borrowing.
- PWLB rates on loans of less than ten years duration are expected to be substantially lower than longer term PWLB rates offering a range of options for new borrowing which will spread debt maturities away from a concentration in long dated debt.
- There is expected to be little difference between 25 year and 50 year rates so therefore loans in the 25-30 year periods could be seen as being more attractive than 50 year borrowing as the spread between the PWLB new borrowing and early repayment rates is considerably less. This would maximise the potential for debt rescheduling and allow the Authority to rebalance its debt maturity profile.
- Consideration will also be given to borrowing fixed rate market loans at 25 – 50 basis points below the PWLB target rate and to maintaining an appropriate balance between PWLB and market debt in the debt portfolio.
- The maturity life of loans are matched to the estimated life of the assets and the MRP repayments which flow from them.

**Sensitivity of the forecast** – In normal circumstances the main sensitivities of the forecast are likely to be the two scenarios noted below. The Authority officers, in conjunction with the treasury advisors, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- *if it were felt that there was a significant risk of a sharp FALL in long and short term rates, e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.*
- *if it were felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.*

### **6.3 External v. internal borrowing**

- This Authority currently has a difference between gross debt and net debt (after deducting cash balances), of £95 million.
- The general aim of this treasury management strategy is to utilise the difference between the two debt levels over the next financial year in order to reduce the credit risk incurred by holding investments. However, measures taken in the last year have already reduced substantially the level of credit risk (see section 7) so another factor which will be carefully considered is the difference between borrowing rates and investment rates to ensure the Authority obtains value for money once an appropriate level of risk management has been attained to ensure the security of its investments.
- The next financial year is expected to be one of historically abnormally low Bank Rate. This provides a continuation of the current window of opportunity for authorities to fundamentally review their strategy of undertaking new external borrowing.
- Over the next three years, investment rates are therefore expected to be below long term borrowing rates and so value for money considerations would indicate that value could best be obtained by avoiding new external borrowing and by using internal cash balances to finance new capital expenditure or to replace maturing external debt (this is referred to as internal borrowing). This would maximise short term savings.
- However, short term savings by avoiding new long term external borrowing in 2010/11 will also be weighed against the potential for incurring additional long term extra costs by delaying unavoidable new external borrowing until later years when PWLB long term rates are forecast to be significantly higher.
- Investment returns have fallen to levels around the 0.25% to 1% mark, but long-term borrowing levels for between 10 and 50 years are generally in a range between 4.50% and 5.00%.
- Given the current level of cash resources, reflecting the fact that substantial borrowings were undertaken in the middle of 2008-09 when it was anticipated that Metrolink 3a would require a similar level of funding, it is unlikely that there will be a need to finance all of the 2010/11 capital expenditure borrowing requirement from

new borrowings. Markets are currently volatile and past months have shown that there are opportunities to obtain longer term funding at advantageous rates for ,sometimes, short periods. In such circumstances, limited borrowings may be undertaken even though there will eventually be a short term cost in holding the monies as short term investments pending their use to fund capital expenditure. Any such short term losses can be met from the capital financing reserve which was created from the extra interest earnings arising during 2008-09 when the difference in rates was reversed.

- Against this background caution will be adopted with the 2010/11 treasury operations. The Treasurer will monitor the interest rate market and adopt a pragmatic approach to changing circumstances, reporting any decisions to the appropriate decision making body at the next available opportunity.

#### **6.4 Policy on borrowing in advance of need**

The Authority will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be considered carefully to ensure value for money can be demonstrated and that the Authority can ensure the security of such funds.

In determining whether borrowing will be undertaken in advance of need the Authority will;

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow
- consider the merits and demerits of alternative forms of funding
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.

#### **7. Debt Rescheduling**

The introduction of different PWLB rates on 1 November 2007 for new borrowing, as opposed to early repayment of debt, and the setting of a spread between the rates applied to new borrowing and repayment of debt, has meant that PWLB to PWLB debt restructuring is now much less attractive than before that date. However, significant interest savings may still be achievable through using LOBOs (Lenders Option Borrowers Option) loans and other market loans in rescheduling exercises.

As short term borrowing rates will be considerably cheaper than longer term rates, there are likely to be significant opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of their short term nature and the likely cost of refinancing those short term loans, once they mature, compared to the current rates of longer term debt in the existing debt portfolio. Any such rescheduling and repayment of debt is likely to cause a flattening of the Authority's maturity profile as in recent years there has been a skew towards longer dated PWLB.

Consideration will also be given to the potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments

are likely to be lower than rates paid on current debt. Reasons for any rescheduling to be undertaken will include:

- the generation of cash savings at minimum risk and without delivering short-term benefits at the expense of longer-term costs;
- to help fulfil the strategy outlined above
- to enhance the balance of the long-term portfolio, e.g. amend the maturity profile and/or the balance of volatility.

There has been much discussion as to whether the size of spread between long term PWLB repayment and new borrowing rates should be revised (downwards) in order to help local authorities currently dissuaded from using investment cash balances to repay long term borrowing and thereby reduce counterparty and interest rate risk exposure. The DMO / PWLB have issued a consultation document with suggested options to revise the methodology used to calculate the early repayment rate. The consultation period ended in January 2010 and this Authority will monitor developments in this area and may amend its strategy if significant changes are introduced.

All rescheduling will be reported to the Authority at the earliest meeting following its action.

## **8. Annual Investment Strategy**

### **8.1 Investment Policy**

The Authority will have regard to the CLG's Guidance on Local Government Investments ("the Guidance") issued in March 2004, any revisions to that guidance, the Audit Commission's report on Icelandic investments and the 2009 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Authority's investment priorities are: -

- (a) the security of capital and
- (b) the liquidity of its investments.

The Authority will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite of this Authority is low in order to give priority to security of its investment.

The borrowing of monies purely to invest or on-lend and make a return is unlawful and this Authority will not engage in such activity.

Investment instruments identified for use in the financial year are listed below. Counterparty limits will be as set through the Treasury Management Practices – Schedules.

These principles would be important in normal circumstances, but the last two years or so have been anything but. The Icelandic banks crisis, which did not impact on the Authority, along with the financial difficulties faced by UK and international banks, have placed security of investments at the forefront of Treasury Management investment policy.

In order to achieve a higher level of security, the Treasurer has introduced a number of measures:-

- Investments to be restricted to UK banks, building societies, local authorities and UK Government institutions. However this will be reviewed during the year and if necessary a report will be presented to the Audit Committee and full Authority for consideration.
- Diversify the investment portfolio into more secure UK government and government backed investment instruments.
- Although current investment strategy allows investments up to 364 days, restrict deposits to as short a time period as feasible.

There is a price to pay for an increased level of security, however. Greater security, and reduced exposure to risk, can only be achieved at the cost of lower rates of return.

Members are asked to note the revised Treasury Management investment strategy.

## 8.2 Specified and Non-Specified Investments

Investment instruments identified for use in the financial year are listed below under 'Specified' and 'Non-Specified' Investments categories.

### Specified Investments

All such investments are sterling denominated, with maturities up to maximum of 1 year, meeting the minimum 'high' rating criteria where applicable.

	<b>Minimum 'High' Credit Criteria</b>	<b>Use</b>
Term deposits – banks and building societies *	See below	In-house
Term deposits – other Local Authorities (LAs)	High security. Only one or two LAs credit rated	In-house
Debt Management Agency Deposit Facility	UK Government Backed	In-house
Nationalised banks	UK Government Backed	In-house
Certificates of deposits issued by banks and building societies covered by UK Government guarantees**	UK Government explicit guarantee	In-house

\* Banks

Have as a minimum the following Fitch (or equivalent) credit ratings (where rated):

- Long Term - Fitch A
- Short Term - Fitch F1
- Support - Fitch 3

Building Societies

Have as a minimum the following Fitch (or equivalent) credit ratings (where rated):

- Long Term - Fitch A-

- ii. Short Term - Fitch F2
- iii. Support - Fitch 3

\*\* Banks supported by the UK bail-out package: -

- Abbey
- Barclays
- HBOS
- Lloyds TSB
- HSBC
- Nationwide Building Society
- RBS
- Standard Chartered

### Non-Specified Investments

Non-specified investments are any other type of investment (i.e. not defined as specified above).

The Authority is not intending to use any non-specified investments.

### **8.3 Investment Limits**

As advised by Sector, our treasury advisers, the financial investment limits of banks and building societies are linked to their Fitch long-term ratings (or Moodys equivalent), as follows:-

#### Banks

Fitch AA+	£10 million
Fitch AA/AA-	£7 million
Fitch A+/A	£5 million

#### Building Societies

Fitch AA/AA-	£15 million
Fitch A+/A-	£10 million

The Debt Management Office has a limit of £200m

District councils have a limit of £5m

Other Local Authorities have a limit of £20m except Manchester City council for which the limit is £50m

### **8.4 Liquidity**

Based on cash flow forecasts, the level of cash balances in 2010-11 is estimated to range between £0m and £95m. The higher level can sometimes arise where, for instance, the Authority takes advantage of favourable long-term interest rates to borrow in advance of need or when large government grants are received.

Giving due consideration to the Authorities' level of balances over the next year, the need for liquidity, its spending commitments and provisioning for contingencies, it is considered

very unlikely that the Authority will have cash balances to invest other than on a temporary basis. For this reason, no cash will be held in term deposit maturities in excess of 1 year.

In some instances it is more cost effective to utilise cash resources to minimise the need for external borrowing. The Treasurer will regularly consider this option.

## 8.5 Creditworthiness policy

This Authority uses the creditworthiness service provided by Sector Treasury Services. This service has been progressively enhanced over the last year and now uses a sophisticated modelling approach with credit ratings from all three rating agencies - Fitch, Moodys and Standard and Poors, forming the core element. However, it does not rely solely on the current credit ratings of counterparties but also uses the following as overlays :-

- credit watches and credit outlooks from credit rating agencies
- CDS spreads to give early warning of likely changes in credit ratings
- sovereign ratings to select counterparties from only the most creditworthy countries

This modelling approach combines credit ratings, credit watches, credit outlooks and CDS spreads in a weighted scoring system for which the end product is a series of colour code bands which indicate the relative creditworthiness of counterparties. These colour codes are also used by the Authority to determine the duration for investments and are therefore referred to as durational bands. The Authority is satisfied that this service now gives a much improved level of security for its investments. It is also a service which the Authority would not be able to replicate using in house resources.

The selection of counterparties with a high level of creditworthiness will be achieved by selection of institutions down to a minimum durational band within Sector's weekly credit list of worldwide potential counterparties. The Authority will therefore use counterparties within the following durational bands: -

- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 3 months

This Authority will not use the approach suggested by CIPFA of using the lowest rating from all three rating agencies to determine creditworthy counterparties as Moodys are currently very much more aggressive in giving low ratings than the other two agencies. This would therefore be unworkable and leave the Authority with few banks on its approved lending list. The Sector creditworthiness service does though, use ratings from all three agencies, but by using a scoring system, does not give undue preponderance to just one agency's ratings.

All credit ratings will be monitored weekly. The Authority is alerted to changes to ratings of all three agencies through its use of the Sector creditworthiness service.

- If a downgrade results in the counterparty/investment scheme no longer meeting the Authority's minimum criteria, its further use as a new investment will be withdrawn immediately.

- In addition to the use of Credit Ratings the Authority will be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Authority's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Authority will also use market data and information, information on government support for banks and the credit ratings of that government support

## **8.6 Country limits**

The Authority has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA+ from Fitch Ratings (or equivalent from other agencies if Fitch does not provide). This list of countries that qualify using this credit criteria will be added to or deducted from by officers should ratings change in accordance with this policy. However this will be reviewed during the year and if necessary a report will be presented to the Audit Committee and full Authority for consideration.

## **8.7 Investment Strategy to be followed in-house**

Bank Rate has been unchanged at 0.50% since March 2009. Bank Rate is forecast to commence rising in quarter 3 of 2010 and then to rise steadily from thereon. Bank Rate forecasts for financial year ends (March) are as follows: -

- **2010** 0.50%
- **2011** 1.50%
- **2012** 3.50%
- **2013** 4.50%

There is downside risk to these forecasts if recovery from the recession proves to be weaker and slower than currently expected.

The Authority will avoid locking into longer term deals while investment rates are down at historically low levels unless exceptionally attractive rates are available which make longer term deals worthwhile.

For 2010/11 the Authority has budgeted for an investment return of 0.65% on investments placed during the financial year.

For its cash flow generated balances, the Authority will seek to utilise its business reserve accounts and short-dated deposits (overnight to three months) in order to benefit from the compounding of interest.

## **8.8 End of year Investment Report**

At the end of the financial year, the Authority will report on its investment activity as part of its Annual Treasury Report.

## **8.9 Policy on the use of external service providers**

The Authority uses Sector Treasury Services and Butlers, both of whom are Manchester City Council's external treasury management advisors.

The Authority recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Authority will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

## **8.10 Scheme of delegation**

To define responsibility to member groups and officers in relation to treasury management.

Please see appendix E.

## **8.11 Role of the section 151 officer**

To define the role of the Treasurer in relation to treasury management.

Please see appendix F.

## **8.12 ITA/PTE Joint Lending Activity**

In order to remove the risk of over exposure by joint lending activities with the same counterparty, it has been agreed with the PTE that they will not invest with any of the other counterparties used by the ITA. Accordingly the PTE will only invest their surplus funds with the Debt Management Office.

## **9. Minimum Revenue Provision (MRP) Strategy**

To outline Authority policy for spreading capital expenditure charge to revenue through the MRP charge.

Please see attached Appendix B

## **10. Recommendations**

See front of report for list of recommendations.

**List of Prudential and Treasury Indicators for approval**

<b>Prudential indicators</b>	<b>2010/11</b>	<b>2011/12</b>	<b>2012/13</b>
<b>Extract from budget setting report</b>	<b>Budget</b>	<b>estimate</b>	<b>estimate</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Capital Expenditure</b>	<b>£417,085</b>	<b>£465,085</b>	<b>£320,060</b>
<b>Ratio of gross financing costs to net revenue stream</b>	<b>15%</b>	<b>17%</b>	<b>23%</b>
<b>Capital Financing Requirement as at 31 March</b>	<b>£575,082</b>	<b>£891,107</b>	<b>£1,148,781</b>
<b>Incremental impact of capital investment on Levy</b>	<b>£4,917</b>	<b>£5,195</b>	<b>£5,494</b>

**Treasury Indicators:**

<b>Maturity structure of fixed rate borrowing during 2010/11</b>	<b>Upper limit</b>	<b>Lower limit</b>
<b>under 12 months</b>	<b>70%</b>	<b>10%</b>
<b>12 months and within 24 months</b>	<b>60%</b>	<b>10%</b>
<b>24 months and within 5 years</b>	<b>60%</b>	<b>0%</b>
<b>5 years and within 10 years</b>	<b>60%</b>	<b>0%</b>
<b>10 years and above</b>	<b>90%</b>	<b>60%</b>

<b>Treasury Indicators</b>	<b>2010/11</b>	<b>2011/12</b>	<b>2012/13</b>
	<b>budget</b>	<b>estimate</b>	<b>estimate</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Authorised Limit for external debt -</b>			
borrowing	<b>£470,502</b>	<b>£795,927</b>	<b>£1,066,615</b>
other long term liabilities	<b>£0</b>	<b>£0</b>	<b>£0</b>
<b>TOTAL</b>	<b>£470,502</b>	<b>£795,927</b>	<b>£1,066,615</b>
<b>Operational Boundary for external</b>			
<b>debt -</b>			
borrowing	<b>£463,502</b>	<b>£788,927</b>	<b>£1,059,615</b>
other long term liabilities	<b>£0</b>	<b>£0</b>	<b>£0</b>
<b>TOTAL</b>	<b>£463,502</b>	<b>£788,927</b>	<b>£1,059,615</b>
<b>Actual external debt</b>	<b>£455,502</b>	<b>£780,927</b>	<b>£1,051,615</b>
<b>Upper limit for fixed interest rate</b>			
<b>exposure</b>			
Net borrowing r.e. fixed rate borrowing as a % of total net borrowing	<b>217%</b>	<b>142%</b>	<b>132%</b>
<b>Upper limit for variable rate</b>			
<b>exposure</b>			
Net borrowing r.e. variable rate borrowing as a % of total net borrowing	<b>61%</b>	<b>77%</b>	<b>80%</b>
<b>Upper limit for total principal sums</b>			
<b>invested for over 364 days</b>	<b>£0</b>	<b>£0</b>	<b>£0</b>

## **Minimum Revenue Policy Strategy**

The Authority is required to make provision for repayment of an element of the accumulated capital spend each year through a revenue charge (the Minimum Revenue Provision), although it is also allowed to undertake additional voluntary payments.

CLG Regulations have been issued, which require the full Authority to approve **an annual MRP Statement**. This will need to be approved in advance of each year. Whilst the regulations revoke current MRP requirements, authorities are allowed to continue historical accounting practice. A variety of options are provided to authorities to replace the existing Regulations, so long as there is a prudent provision. The timetable for implementation is very tight and so Members are asked to approve the following policy, based on the Regulations.

Based on the regulations, the Authority is recommended to approve the following MRP Statement for application in both 2009-10 and 2010-11 :-

- For capital expenditure incurred on non Metrolink and non Transport Delivery Programme schemes, MRP will continue to be calculated at 4% of the previous year end's Capital Adjustment Account, using the former CLG Regulations 28 and 29.
- For capital expenditure incurred on the Metrolink and Transport Delivery Programme schemes, MRP will be deferred until the year after the asset has been commissioned into use. The MRP start years are as follows :
  - Metrolink 3a – Chorlton line, N/A as fully DfT funded.
  - Metrolink 3a - Oldham line Queens Road to Central Park, N/A as fully DfT funded.
  - Metrolink 3a – Oldham line Central Park to Oldham Mumps 2012-13.
  - Metrolink 3a – Oldham line Oldham Mumps to Rochdale 2012-13.
  - Metrolink 3a –Droylsden line 2012-13.
  - Metrolink SEP/SIP – between 2008-09 and 2012-13.
  - Transport Delivery Programme – between 2013-14 and 2017-18.
- The new regulation provides that the MRP Statement can be revised by the Authority at any stage. It is possible that such a revision will be necessary once the detailed funding of Metrolink 3a and the Transport Delivery Programme has been finalised.

**Treasury Management Policy Statement**

1. This organisation defines its treasury management activities as: “The management of the authority’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 organisation 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 organisation.
3. This organisation 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.”

## **Adoption of revised CIPFA Treasury Management Code of Practice 2009**

### **INTRODUCTION**

The CIPFA Code of Practice on Treasury Management in Local Authorities was last updated in 2001 and has been revised in 2009 in the light of the default by Icelandic banks in 2008. The revised Code requires that a report be submitted to the Authority, board or other appropriate body, setting out four amended clauses which should be formally passed in order to approve adoption of the new version of the Code of Practice and Cross-Sectoral Guidance Notes.

The revised Code also includes an amended version of the treasury management policy statement (TMPS) incorporating just three clauses and a revised definition of treasury management activities. The Code does not require this statement to be approved by the Authority, board or other appropriate body.

The revised Code has also set out various requirements which have been summarised in paragraph 1 of the latest Treasury Management Strategy Statement.

### **RESOLUTIONS**

CIPFA recommends that all public service organisations adopt, as part of their standing orders, financial regulations, or other formal policy documents appropriate to their circumstances, the following four clauses.

1. This organisation will create and maintain, as the cornerstones for effective treasury management:

- a treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities
- suitable treasury management practices (TMPs), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of this organisation. Such amendments will not result in the organisation materially deviating from the Code's key principles.

2. This organisation (i.e. Authority) will receive reports on its treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMPs.

3. This organisation delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Audit Committee, and for the execution and administration of treasury management decisions to the Treasurer, who will act in accordance with the organisation's policy statement and TMPs and, if he is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

4. This organisation nominates Audit Committee responsible for ensuring effective scrutiny of the treasury management strategy and policies.

**Treasury management scheme of delegation**

**(i) Full Authority**

- receiving and reviewing reports on treasury management policies, practices and activities
- approval of annual strategy.

**(ii) Responsible body – Audit Committee**

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices
- budget consideration and approval
- approval of the division of responsibilities
- receiving and reviewing regular monitoring reports and acting on recommendations
- approving the selection of external service providers and agreeing terms of appointment.

**(iii) Body with responsibility for scrutiny - Audit Committee**

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

**(iv) Treasurer**

- delivery of the function

**The treasury management role of the section 151 officer**

**The S151 (responsible) officer**

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers.

## **Economic Background**

### **1. Introduction**

- The credit crunch storm of August 2007 eventually fed through to the near collapse of the world banking system in September 2008. This then pushed most of the major economies of the world into a very sharp recession in 2009 accompanied by a dearth of lending from banks anxious to rebuild their weakened balance sheets. Many governments were forced to recapitalise and rescue their major banks and central banks precipitately cut their central bank rates to 0.10 – 1.00% in order to counter the recession.
- The long awaited start of growth eventually came in quarter 3 2009 in the US and the EU. However, there was disappointment that the UK failed to emerge from recession in quarter 3.
- Inflation has plunged in most major economies and is currently not seen as being a problem for at least the next two years due to the large output gaps and high unemployment putting a lid on wage growth. In many countries there have been widespread pay freezes in 2009 and these are likely to be persistent for some time.
- Deflation could become a threat in some economies if they were to go into a significant double dip recession.
- Asian countries, especially China, are buoying world demand through their own stimulus measures.
- There still needs to be a radical world rebalancing of excess savings rates by cash rich Asian and oil based economies and excess consumption rates in Western economies if the world financial system is not to avoid a potential rerun of this major financial crisis in years to come.
- Most major economies have resorted to a huge expansion of fiscal stimulus packages in order to encourage a fast exit from recession. This, together with expenditure on direct support provided to ailing banks, has led to a drastic expansion in government debt levels which will take many years to eliminate and to restore the previous health of national finances.

### **2 Two growth scenarios**

- The current big issue is 'how quickly will the major world economies recover?' There is a sharp division of opinion on this question as set out below. The knock on effects on forecasts for interest rates can be seen in appendix H – UBS strong recovery, Capital Economics – weak recovery.

#### **2.1 Strong recovery**

- This is a normal cyclical recovery which will be strong in the major world economies. The US still has potential to add further fiscal stimulus in 2010 to ensure that strong recovery continues after the current round of stimulus measures end. Growth in the EU is likely to be strong in 2010 and not require such help.

## **The UK:**

- GDP growth will almost get back to the long term average of about 2.5% in 2011 but is likely to peak in the first half of the year as inventory rebuilding and stimulus measures fade and fiscal contraction kicks in later in the year.
- The economy will rebalance with strong growth in exports and import substitution helped by strong recovery in the EU and the rest of the world.
- Sterling has depreciated by 25% since the peak in 2007 and is likely to stay weak.
- Consumer spending – only a mediocre recovery is expected due to a steady increase in the savings ratio from +5.6% in 2009 to about 8% in 2011 as consumers pay down debt or build cash balances. Consumer incomes will be held down by wage freezes and increases in taxation.
- House price recovery is expected to persist helped by a low Bank Rate for a prolonged period; the peak to trough fall in house prices is now expected to be no more than 20%. House prices to rise by about 6% in 2010, and 3% in 2011; mortgage approvals will rise back to the level of 75 - 80,000 per month needed to ensure a continuation of a trend of rising house prices.
- CPI inflation to peak @ 2.5% in early 2010 after the rise in VAT in January but then to fall to a trough near 1.5% in early 2011 and to stay below 2% for the rest of 2011.
- The current MPC attitude is one of hang on as long as possible before increasing Bank Rate. The aim of this would be to try to ensure that growth gets going at a decent rate and that Bank Rate gets back to 4 – 5% before the next recession and that all assets purchased through QE have been sold off by then. The first Bank Rate increase is expected in Q3 2009.
- If there is a change of Government in 2010 with a more aggressive fiscal approach then this could delay the timing of Bank Rate starting to go up.
- The fiscal deficit is 6.4% of GDP, about £90bn, which is expected to fall at £11bn p.a. over eight years at currently planned rates. This is similar to the peak deficit of 7% in 1990s which was remedied to a surplus of 1.6% in the space of 6 years helped by strong, steady economic growth of 3% p.a. supported by loose monetary policy that compensated for the fiscal squeeze.
- Gilt yields, especially longer term ones, are currently artificially low due to the Bank of England's Quantitative Easing operations. £200bn of gilts, commercial bonds and paper are being purchased under this scheme which has inflated prices and depressed yields. Once this campaign ends, yields will inevitably rise but will also rise due to the huge level of issuance of new gilts to finance the fiscal deficit. Long gilt yields are therefore forecast to reach 6% during 2011.
- Gilt yields could rise higher if there was a hung Parliament in 2010 or if the fiscal situation deteriorates further.
- The major risk to this scenario would be a lack of supply of bank credit. However, it is felt that the Bank of England is on alert to ensure that this does not happen and would continue various measures to assist the expansion of credit.

## **2.2 Weak recovery**

- The current economic cycle is not a normal business cycle but a balance sheet driven cycle. Over borrowed banks, corporates and consumers are focused on shrinking their levels of borrowing to more viable and affordable levels and this balance sheet adjustment will take several years to be effected. Repayment of debt will therefore act as a major head wind to the required increase in demand in the economy.

Consequently there will only be weak economic recovery over the next few years after the initial sharp inventory rebuilding rebound fades. GDP growth is forecast to reach only +1.5% in 2011.

- Fiscal contraction will further dampen economic recovery driven by a strong political agenda to accelerate cuts in expenditure and increases in taxation after the general election in 2010.
- The consumer savings ratio will rise so as to eliminate over borrowing and to insure against people losing their jobs during this downturn. This will depress consumer expenditure, the main driver of the UK economy.
- Growth will also be hampered by a reduced supply of credit from weakened banks compounded by weak demand for credit.
- The eventual reversal of Quantitative Easing will take cash out of the economy and reduce demand in the economy.
- Unemployment is likely to rise to near to 3m in 2010 and take years to subside due to weak growth. High unemployment will reduce tax income and increase expenditure on benefits and the costs of local authority services.
- Inflation will not be a threat for several years as the current 6% output gap will take until 2014 to be eliminated.
- However, deflation is a major danger for some years: the major falls in manufacturing prices over the last 12 -18 months have still to feed through to the economy and then to impact wage deflation.
- CPI inflation will blip up over 2% in early 2010 but will then be on a strong downward trend to about -1% in 2011.
- There is no need for the MPC to change Bank Rate from 0.5% in 2010 or 2011 and possibly for 5 years as they will need to counter the fiscal contraction which will dampen demand in the economy.
- Long PWLB rates will FALL from current levels to near 4% in 2010 due to weak economic recovery and minimal inflation so that the real rate of return (net of inflation) on long gilts is healthy at these low levels

### 2.3 Sector view

- Sector recognises that at the current time it is difficult to have confidence as to exactly how strong the UK economic recovery will prove to be. Both the above scenarios are founded on major assumptions and research which could or could not turn out to be correct.
- Sector has adopted a more moderate view between these two scenarios outlined above i.e. a moderate return to growth.
- We do, however, feel that the risks that long term gilt yields and PWLB rates will rise markedly are high.
- There are huge uncertainties in all forecasts due to the major difficulties of forecasting the following areas: -
  - degree of speed and severity of fiscal contraction after the general election
  - timing and amounts of the reversal of Quantitative Easing,
  - speed of recovery of banks' profitability and balance sheet imbalances
  - changes in the consumer savings ratio
  - rebalancing of the UK economy towards exporting and substituting imports

- The overall balance of risks is weighted to the downside i.e. the pace of economic growth disappoints and Bank Rate increases are delayed and / or lower
- There is an identifiable risk of a double dip recession and deleveraging creating a downward spiral of falling demand, falling jobs and falling prices and wages leading to deflation but this is considered to be a small risk and an extreme view at the current time on the basis of current evidence

**Prospects for Interest Rates**

The data below shows a variety of forecasts published by a number of institutions, they are individual forecasts including those of UBS and Capital Economics (an independent forecasting consultancy).

The forecast within this strategy statement has been drawn from these diverse sources and officers' own views.

**1. INDIVIDUAL FORECASTS**

**Sector interest rate forecast – 23.11.09**

	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13
Bank rate	0.50%	0.50%	0.75%	1.00%	1.50%	2.25%	2.75%	3.25%	3.50%	3.75%	4.25%	4.25%	4.50%
5yr PWLB rate	3.05%	3.20%	3.30%	3.40%	3.60%	3.85%	4.15%	4.55%	4.60%	4.80%	4.80%	4.85%	4.85%
10yr PWLB rate	4.00%	4.05%	4.15%	4.30%	4.45%	4.60%	4.80%	4.90%	5.00%	5.10%	5.10%	5.15%	5.15%
25yr PWLB rate	4.55%	4.65%	4.70%	4.80%	4.90%	5.00%	5.05%	5.10%	5.20%	5.30%	5.30%	5.35%	5.35%
50yr PWLB rate	4.60%	4.70%	4.75%	4.90%	5.00%	5.10%	5.15%	5.20%	5.30%	5.40%	5.40%	5.45%	5.45%

**Capital Economics interest rate forecast – 18.1.10**

	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11
Bank Rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%
5yr PWLB rate	3.15%	2.95%	2.65%	2.45%	2.45%	2.45%	2.45%	2.45%
10yr PWLB rate	4.45%	4.15%	3.65%	3.15%	3.15%	3.15%	3.15%	3.15%
25yr PWLB rate	4.75%	4.65%	4.35%	4.05%	3.95%	3.75%	3.75%	3.75%
50yr PWLB rate	4.65%	4.65%	4.25%	4.25%	4.25%	4.25%	4.25%	4.25%

**UBS interest rate forecast (for quarter ends) – 30.10.09**

	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11
Bank Rate	0.50%	0.50%	0.75%	1.00%	1.50%	2.00%	2.50%	3.00%
10yr PWLB rate	3.90%	4.05%	4.40%	4.75%	4.90%	5.15%	5.40%	5.40%
25yr PWLB rate	4.45%	4.65%	5.00%	5.15%	5.40%	5.65%	5.90%	5.90%
50yr PWLB rate	4.55%	4.75%	5.10%	5.25%	5.50%	5.75%	6.00%	6.00%

## **Glossary of Terms**

**Authorised Limit** - This Prudential Indicator represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable. It is the expected maximum borrowing need, with some headroom for unexpected movements.

**Bank Rate** – the rate at which the Bank of England offers loans to the wholesale banks, thereby controlling general interest rates in the economy.

**Counterparty** – one of the opposing parties involved in a borrowing or investment transaction

**Credit Rating** – A qualified assessment and formal evaluation of an institution's (bank or building society) credit history and capability of repaying obligations. It measures the probability of the borrower defaulting on its financial obligations, and its ability to repay these fully and on time.

**Discount** – Where the prevailing interest rate is higher than the fixed rate of a long-term loan, which is being repaid early, the lender can refund the borrower a discount, the calculation being based on the difference between the two interest rates over the remaining years of the loan, discounted back to present value. The lender is able to offer the discount, as their investment will now earn more than when the original loan was taken out.

**Fixed Rate Funding** - A fixed rate of interest throughout the time of the loan. The rate is fixed at the start of the loan and therefore does not affect the volatility of the portfolio, until the debt matures and requires replacing at the interest rates relevant at that time.

**Gilts** - The loan instruments by which the Government borrows. Interest rates will reflect the level of demand shown by investors when the Government auctions Gilts.

**High/Low Coupon** – High/Low interest rate

**Liquidity** – The ability of an asset to be converted into cash quickly and without any price discount. The more liquid a business is, the better able it is to meet short-term financial obligations.

**Market** - The private sector institutions - Banks, Building Societies etc.

**Maturity Profile/Structure** - an illustration of when debts are due to mature, and either have to be renewed or money found to pay off the debt. A high concentration in one year will make the Authority vulnerable to current interest rates in that year.

**Monetary Policy Committee** – the independent body that determines Bank Rate.

**Operational Boundary** – This Prudential Indicator is based on the probable external debt during the course of the year. It is not a limit and actual borrowing could vary around this boundary for short times during the year. It should act as an indicator to ensure the

Authorised Limit is not breached.

**Premium** – Where the prevailing current interest rate is lower than the fixed rate of a long-term loan, which is being repaid early, the lender can charge the borrower a premium, the calculation being based on the difference between the two interest rates over the remaining years of the loan, discounted back to present value. The lender may charge the premium, as their investment will now earn less than when the original loan was taken out.

**Prudential Code** - The Local Government Act 2003 requires the Authority to ‘have regard to’ the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Authority’s capital investment plans are affordable, prudent and sustainable.

**PWLB** - Public Works Loan Board. Part of the Government’s Debt Management Office, which provides loans to public bodies at rates reflecting those at which the Government is able to sell Gilts.

**Specified Investments** - Sterling investments of not more than one-year maturity. These are considered low risk assets, where the possibility of loss of principal or investment income is very low.

**Non-specified investments** - Investments not in the above, specified category, e.g., foreign currency, exceeding one year or outside our minimum credit rating criteria.

**Variable Rate Funding** - The rate of interest either continually moves reflecting interest rates of the day, or can be tied to specific dates during the loan period. Rates may be updated on a monthly, quarterly or annual basis.

**Volatility** - The degree to which the debt portfolio is affected by current interest rate movements. The more debt maturing within the coming year and needing replacement, and the more debt subject to variable interest rates, the greater the volatility.

**Yield Curve** - A graph of the relationship of interest rates to the length of the loan. A normal yield curve will show interest rates relatively low for short-term loans compared to long-term loans. An inverted Yield Curve is the opposite of this.