

AUDIT AND GOVERNANCE COMMITTEE

11 February 2011

**TREASURY MANAGEMENT POLICY AND STRATEGY 2011/2012,
INCLUDING PRUDENTIAL 'TREASURY MANAGEMENT' INDICATORS FOR
2011/2012 TO 2013/2014**

Report of the Executive Director of Commercial and Corporate Services

1. Purpose of the Report

- 1.1 To inform the Audit and Governance Committee on the Treasury Management Policy and Strategy (including both borrowing and investment strategies) proposed for 2011/2012 and to note the Prudential 'Treasury Management' Indicators for 2011/2012 to 2013/2014 and to provide comments to Cabinet and Council on the proposed policy and indicators where appropriate.

2. Description of Decision

- 2.1 Committee is requested to:
- Provide any appropriate comments to Cabinet / Council on the proposed:
 - Annual Treasury Management Policy and Strategy (including specifically the Annual Borrowing and Investment Strategies);
 - prudential 'Treasury Management' indicators;

3. Treasury Management

- 3.1 Treasury management is defined as "the management of the local 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."

3.2 Statutory requirements

The Local Government Act 2003 (the Act) and supporting regulations requires the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Management Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable, these are set out in Appendix 1.

The Act also requires the Council to adopt a Treasury Management Policy Statement (detailed in Appendix 2) and to set out its Treasury

Management Strategy comprising the Council's strategy for borrowing and the Council's policies for managing its investments and giving priority to the security and liquidity of those investments (Appendix 3).

The Department of Communities and Local Government issued revised investment guidance which came into effect from 1 April 2010. There are no major changes required over and above the arrangements that the Council already has in place and were included in the revised CIPFA Treasury Management Code of Practice 2009 that the Council fully adheres to.

3.3 CIPFA requirements

The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised November 2009) was adopted by this Council on 3rd March 2010.

The primary requirements of the Code are as follows:

1. The Council 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 (TMP's), 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 (is detailed in Appendix 2) and the TMP's follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the Council. Such amendments which are minor in nature do not result in the Council deviating from the Code's key principles however.

2. The Council will receive reports on 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 TMP's.

3. The Council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Cabinet, and for the execution and administration of treasury management decisions to the Executive Director of Commercial and Corporate Services, who acts in accordance with the organisation's Policy Statement, TMPs and CIPFA's Standard of Professional Practice on Treasury Management.

4. The Council has previously nominated the Audit and Governance Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

Treasury Management Strategy for 2011/2012

- 3.4 The Treasury Management Strategy comprises a Borrowing and an Investment Strategy. These set out the Council's policies for managing its borrowing and investments and for giving priority to the security and liquidity of investments.
- 3.5 There are no major changes being proposed to the overall Treasury Management Strategy in 2011/2012 which maintains the careful and prudent approach adopted by the Council in previous years. Particular areas that inform the strategy include the extent of potential borrowing included in the Council's capital programme, the availability of borrowing, and the current and forecast world and UK economic position, in particular forecasts relating to interest rates and security of investments.
- 3.6 The proposed Treasury Management Strategy Statement for 2011/2012 is set out in Appendix 3 and is based upon the views of the Executive Director of Commercial and Corporate Services, supplemented with market data, market information and leading market forecasts provided by the Council's treasury adviser, Sector Treasury Services.
- 3.7 The strategy is subject to regular review to ensure compliance to the agreed treasury management strategy and that the strategy adapts to changing financial markets as appropriate. It is pleasing to note that the Council's current average rate of borrowing at 3.35% is low in comparison with other local authorities whilst the current rate earned on investments at 1.49% is higher than the benchmark rate. In addition debt rescheduling undertaken by the Council has achieved significant savings in interest charges and discounts and these interest savings have been secured for many years to come. For example, since November 2008 the Council has rescheduled debt worth £59.5 million with an ongoing reduction in interest costs of just under £1.0 million per annum. Market conditions are under constant review so that the Council can take a view on the optimum time to carry out further borrowing or debt rescheduling.

4. Suggested Reason for Decision

- 4.1 To comply with statutory requirements.

5. Alternative Options

- 5.1 No alternatives are submitted for Cabinet consideration

Background Papers

Sector City Watch (Monthly)

Local Government Act 2003

The Prudential Code for Capital Finance in Local Authorities (Fully Revised Second Edition)

Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes (Fully Revised Second Edition 2009)

Treasury Management in the Public services Guidance Notes for Local Authorities including Police Authorities and Fire Authorities (Fully Revised Third Edition)

Prudential 'Treasury Management' Indicators 2011/2012 to 2013/2014

The indicators below relate to Treasury Management (all indicators relating to capital financing have been removed for clarity and can be found in the Capital Programme 2011/2012 and Treasury Management Policy and Strategy 2011/2012, including Prudential Indicators for 2011/2012 to 2013/2014 report to Cabinet - 16th February 2011.

- P5 In respect of its external debt, it is recommended that the Council approves the following authorised limits for its total external debt, gross of investments for the next three financial years, and agrees the continuation of the previously agreed limit for the current year since no change to this is necessary. These limits separately identify borrowing from other long-term liabilities such as PFI schemes and finance leases. The Council is asked to approve these limits and to delegate authority to the Executive Director of Commercial and Corporate Services, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities, in accordance with option appraisal and best value for the authority. Any such changes made will be reported to Cabinet and the Council at the next meetings following the change.

	Authorised Limit for External Debt			
	2010/11	2011/12	2012/13	2013/14
	£000	£000	£000	£000
Borrowing	323,990	331,539	340,096	347,623
Other long term liabilities	91,558	50,860	48,710	46,515
Total	415,548	382,399	388,806	394,138

The Executive Director of Commercial and Corporate Services reports that these authorised limits are consistent with the Authority's current commitments, existing plans and the proposals in this report for capital expenditure and financing, and with its approved treasury management policy statement and practices. The Executive Director of Commercial and Corporate Services also confirms that they are based on the estimate of most likely, prudent, but not worst case scenario, with, in addition, sufficient headroom over and above this to allow for operational management, for example unusual cash movements. Risk analysis and risk management strategies have been taken into account, as have plans for capital expenditure, estimates of the Capital Financing Requirement and estimates of cash flow requirements for all purposes. It should be noted that the Council undertakes investment and borrowing on behalf of external bodies such as Tyne and Wear Fire and Rescue Authority. Treasury Management undertaken on behalf of other authorities is included in Sunderland's borrowing limits, however it is excluded when considering financing costs and when calculating net borrowing for the

Council. A specific element of risk has also been taken into account for these bodies.

In taking its decisions on the Revenue Budget and Capital Programme for 2011/2012, the Council is asked to note that the authorised limit determined for 2011/2012, (see P5 above), will be the statutory limit determined under section 3(1) of the Local Government Act 2003.

- P6 The Council is also asked to approve the following operational boundary for external debt for the same time period and agrees the continuation of the previously agreed limit for the current year since no change to this is necessary. The proposed operational boundary for external debt is based on the same estimates as the authorised limit, but reflects directly the estimate of the most likely, prudent but not worst case scenario level, without the additional headroom included within the authorised limit to allow for example for unusual cash movements, and equates to the maximum of external debt projected by this estimate. The operational boundary represents a key management tool for in year monitoring. Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified. The Council is also asked to delegate authority to the Executive Director of Commercial and Corporate Services, within the total operational boundary for any individual year, to effect movement between the separately agreed figures for borrowing and other long term liabilities, similar to the authorised limit set out above.

The operational boundary limit will be closely monitored and a report will be made to Cabinet and Council if it is exceeded at any point. In any financial year, it is generally only expected that the actual debt outstanding will approach the operational boundary when all of the long-term borrowing has been undertaken for that particular year and will only be broken temporarily as a result of the timing of debt rescheduling.

	Operational Boundary for External Debt			
	2010/11	2011/12	2012/13	2013/14
	£000	£000	£000	£000
Borrowing	235,743	261,603	276,335	291,258
Other long term liabilities	91,558	50,860	48,710	46,515
Total	327,301	312,463	325,045	337,773

- P7 The Council's actual external debt at 31st March 2010 was £178.273 million.

The Council includes an element for long-term liabilities relating to PFI schemes and finance leases in its calculation of the operational and authorised boundaries to allow further flexibility over future financing. It should be noted that actual external debt is not directly comparable to the authorised limit and operational boundary, since the actual external debt reflects the position at any one point in time and allowance needs to be made for cash flow variations.

- P9 The Council is also required to indicate if it has adopted the CIPFA Code of Practice on Treasury Management. This original 2001 Code was adopted on 20th November 2002 by full Council and the revised Code was adopted on 3rd March 2010.

The objective of the Prudential Code is to provide a clear framework for local authority capital finance that will ensure for individual local authorities that:

- (a) capital expenditure plans are affordable;
- (b) all external borrowing and other long term liabilities are within prudent and sustainable levels;
- (c) treasury management decisions are taken in accordance with professional good practice;

and that in taking decisions in relation to (a) to (c) above the local authority is

- (d) accountable, by providing a clear and transparent framework.

Further, the framework established by the Code should be consistent with and support:

- (e) local strategic planning;
- (f) local asset management planning;
- (g) proper option appraisal.

In exceptional circumstances the objective of the Code is to provide a framework that will demonstrate that there is a danger of not ensuring the above, so that the Authority can take timely remedial action.

- P10 It is recommended that the Council sets an upper limit on its fixed interest rate exposures of £105 million in 2011/2012, £125 million in 2012/2013 and £145 million in 2013/2014.

- P11 It is further recommended that the Council sets an upper limit on its variable interest rate exposures of £60 million in 2011/2012, £60 million in 2012/2013 and £50 million in 2013/2014.

- P12 It is recommended that the Council sets upper and lower limits for the maturity structure of its borrowings as follows:

Amount of projected borrowing that is fixed rate maturing in each period expressed as a percentage of total projected borrowing that is fixed rate at the start of the period:

	Upper limit	Lower limit
Under 12 months	50%	0%
12 months and within 24 months	60%	0%
24 months and within 5 years	80%	0%
5 years and within 10 years	100%	0%
10 years and within 20 years	100%	0%
20 years and within 30 years	100%	0%
30 years and within 40 years	100%	0%
40 years and within 50 years	100%	0%
over 50 years	100%	0%

P13 A maximum maturity limit of £100 million is set for each financial year (2011/2012, 2012/2013 and 2013/2014) for long term investments, (those over 364 days), made by the authority. This gives additional flexibility to the Council in undertaking its Treasury Management function. Should the Council appoint any external fund managers during the year, these limits will be apportioned accordingly. The type of investments to be allowed are detailed in the Annual Investment Strategy (Appendix 3).

At present the Council has £0.836 million of long-term investments. This is £0.816 million for the value of share capital held in NIAL Holdings PLC. This equates to a 9.41% share in Newcastle International Airport. The Council also holds £0.020 million in government securities, other shares and unit trusts.

Treasury Management Policy Statement

In line with CIPFA recommendations, on the 3rd March 2010 the Council adopted the following Treasury Management Policy Statement, which defines the policies and objectives of its treasury management activities:

- The Council defines its treasury management activities as: The management of the Council's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".
- The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.
- The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

The Council needs to re-affirm its commitment to the above Treasury Management Policy Statement each year.

Treasury Management Strategy Statement for 2011/2012

1. Introduction

- 1.1 The Local Government Act 2003 and subsequent guidance requires the Council to set out its Treasury Management Strategy for Borrowing and to prepare an Annual Investment Strategy. This sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

The suggested strategy for 2011/2012 is set out below and is based upon the Executive Director of Commercial and Corporate Services views on interest rates, supplemented with leading market forecasts and other financial data available and advice provided by the Council's treasury adviser, Sector Treasury Services.

- 1.2 The treasury management strategy covers:

A. Borrowing Policy and Strategy

- treasury limits for 2011/2012 to 2013/2014
- the past and current treasury management position
- the borrowing requirement 2011/2012
- prudential and treasury management Indicators for 2011/12 to 2013/14
- prospects for interest rates
- the borrowing strategy
- policy on borrowing in advance of need
- debt rescheduling

B. Annual Investment Policy and Strategy

- Investment policy and objectives
- the investment strategy
- investment types
- investments defined as capital expenditure
- investment limits
- provision for credit related losses
- creditworthiness policy
- monitoring of credit ratings
- past performance and current position
- outlook and proposed investment strategy
- external fund managers
- policy on use of external service providers

2. Borrowing Policy and Strategy

2.1 Treasury Limits for 2011/12 to 2013/14

It is a statutory duty under Section 3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under

review how much it can afford to borrow. The amount so determined is termed the “Affordable Borrowing Limit”. In England and Wales the Authorised Limit represents the legislative limit specified in the Act.

The Council 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 council tax and council rent levels is ‘acceptable’.

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 set, on a rolling basis, for the forthcoming financial year and two successive financial years and details can be found in Appendix 1 of this report. The Council is asked to approve these limits and to delegate authority to the Executive Director of Commercial and Corporate Services, within the total limit for any individual year, to action movement between the separately agreed limits for borrowing and other long term liabilities where this would be appropriate. Any such changes made will be reported to the Cabinet and the Council at their next meetings following the change.

Also, the Council is asked to approve the Operational Boundary Limits which are included in the Prudential Indicators (Appendix 1). This operational boundary represents a key management tool for in year monitoring. Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified and the Council is also asked to delegate authority to the Executive Director of Commercial and Corporate Services, within the total operational boundary for any individual year, to action movement between the separately agreed figures for borrowing and other long-term liabilities, in a similar fashion to the authorised limit.

2.2 The Past and Current Treasury Management Position

2.2.1 Interest Rates 2010/2011

Interest rates were fairly static with only small variations during the current financial year, until the government, on 20th October 2010, following the Chancellor’s announcement of the Spending Review, instructed the PWLB to increase the average interest rate on all new loans by an average of 1.00% above the Government’s cost of borrowing. This unexpected change at the time saw an overall increase in all PWLB rates going forward of 0.87% making borrowing from this source both less affordable and less attractive. The table below shows that the largest movement in rates was short term borrowing up to one year of 0.82% and by approximately 0.5% on all other maturity periods. Rates increased because of the government’s actions but there has been a slow fall in interest rates since. This trend is starting to reverse but no significant movements are anticipated for the next financial year. This position will be carefully monitored however.

Loan Type	31 st March 2010 %	31 st December 2010 %	Difference %
7 Day Notice	0.30	0.40	0.10
1 Month	0.42	0.45	0.03
PWLB – 1 Year	0.83	1.65	0.82
5 Year	2.89	3.33	0.44
10 Years	4.19	4.58	0.39
25 Years	4.67	5.23	0.56
50 Years	4.70	5.16	0.46

The Bank of England Base Rate has remained at 0.50% since 5th March 2009 with little sign that it will be raised in the short term.

2.2.2 Long Term Borrowing 2010/2011

The Treasury Management Policy and Strategy Statement for 2010/2011 included a benchmark rate of 4.5% for all long-term borrowing.

The Council's strategy for 2010/2011 is to adopt a pragmatic approach and to respond to any changing circumstances to seek to secure benefit for the Council. In response to the Government's increase in PWLB rates across all PWLB loan periods, the Council's benchmark rate for long-term borrowing was increased to 5.5% for the remainder of 2010/2011.

So far in 2010/2011 £30.50 million of long term borrowing has been undertaken at an average rate of 3.31% (£26.5m in respect of debt rescheduling carried out in earlier years, £3.5m for approved prudential borrowing and £0.5m in respect of a specific loan taken out on behalf of Beamish Museum), details of the new loans are shown below. It is pleasing to report that the replacement borrowing was made before the government unexpectedly and immediately increased borrowing rates by on average 1% across all loan duration periods on 20th October 2010, the date of the Spending Review.

Long Term PWLB Borrowing 2010/2011						
Date	Amount £m	Period (Years)	Rate %	Benchmark Rate %	Margin %	Loan Type
11/05/10	0.5	15	3.65	4.50	0.85	EIP*
25/05/10	10.0	4	1.99	4.50	2.51	Maturity
25/05/10	5.0	50	4.29	4.50	0.21	Maturity
27/07/10	5.0	11	3.75	4.50	1.25	Maturity
27/07/10	5.0	12	3.87	4.50	1.13	Maturity
01/09/10	5.0	50	3.96	4.50	0.54	Maturity
	30.5		3.31			

*This loan was taken out on behalf of Beamish Museum and is an Equal Instalment of Principal (EIP) loan

The Council also has nine market, Lender's Option / Borrower's Option (LOBO's), loans totalling £39.5 million. The lender has the option to alter the rate on these loans at set intervals and the Council can either accept the new rate or repay the loan without penalty. If interest rates begin to rise the council will need to consider the potential to have to replace these loans. The following table shows the LOBO's that were subject to a potential rollover in this financial year but have not been replaced as the option was not exercised.

<u>Roll Over Dates</u>	<u>Lender</u>	<u>Amount £m</u>	<u>Rate %</u>	<u>Roll Over Periods</u>
23/04/2010 and 23/10/2010	Barclays	5.0	4.50	Every 6 months (Variable Rate)
14/08/2010	Barclays	5.0	4.45	Every 3 years (Fixed Rate)
Total		10.0		

2.2.3 Current Portfolio Position

The Council's treasury portfolio position at 31st December 2010 comprised:

		Principal (£m)	Total (£m)	Average Rate (%)
Borrowing				
Fixed Rate Funding	PWLB	138.0		
	Market (LOBO's)	34.5		
	Other	0.4	172.9	3.86
Variable Rate Funding	PWLB	0.0		
	Market (LOBO's)	5.0		
	Temporary/Other	31.1	36.1	0.92
Total Borrowing			209.0	3.35
Total Investments	In House		214.1	1.49
Net Position			(5.1)	

The Council currently has a difference between gross debt and net debt of £5.1 million, however this position is expected to change over the next few years as the Council has to manage its finances with significantly less government grant in both capital and revenue funding which could impact in the form of increased borrowing and possible temporary reductions to reserves, with the result that total borrowing could then exceed investments.

There are a number of risks and benefits associated with having both a large amount of debt whilst at the same time having a considerable amount of investments.

Benefits of having a high level of investments are;

- liquidity risk – having a large amount of investments means that the Council is at less of a risk should money markets become restricted or borrowing less generally available, this mitigates against liquidity risk;
- interest is received on investments which helps the Council to address its Strategic Priorities;
- the Council has greater freedom in the timing of its borrowing as it can afford to wait until the timing is right rather than be subject to the need to borrow at a time when interest rates are not advantageous.

Risks associated with holding a high level of investments are;

- the Counterparty risk – institutions cannot repay the Council investment placed with them;
- interest rate risk – the rate of interest earned on the investments will be less than that paid on debt, thus causing a loss to the Council.

The Council has mitigated these risks by formulating its Treasury Management Policy that incorporates both a Borrowing Strategy and an Annual Investment Strategy and has also taken prudent action to redeem debt early by temporarily using investments to the benefit of the Council and saving on interest charges when opportunities have arisen.

2.3 Borrowing Requirement 2011/2012

The Council's borrowing requirement is as follows:

	2011/12 £m	2012/13 £m	2013/14 £m
1. Capital Borrowing (potential)	47.7	15.0	15.0
2. Replacement borrowing (PWLB)	0.0	5.0	5.0
3. Replacement borrowing (Market)	0.0	0.0	0.0
4. Market LOBO replacement (potential)	19.5	20.0	10.0
TOTAL – KNOWN (2+3)	0.0	5.0	5.0
TOTAL – POTENTIAL (1+4)	67.2	35.0	25.0

2.4 Prudential and Treasury Management Indicators for 2011/12 – 2013/14

Prudential and Treasury Indicators (as set out in Appendix 1) are a requirement of the CIPFA Prudential Code and are relevant for the purposes of setting an integrated treasury management strategy and to

ensure that treasury management decisions are taken in accordance with good professional practice.

The Council is also required to indicate if it has adopted the CIPFA Code of Practice on Treasury Management. The original 2001 Code was adopted on 20th November 2002 and the revised 2009 Code was adopted by the full Council on 3rd March 2010. The Council also re-affirms its full adherence to the code annually (as set out in Appendix 5).

2.5 Prospects for Interest Rates

The Council's treasury advisors are Sector Treasury Services and part of their service is to assist the Council to formulate a view on interest rates. A number of current City forecasts for short term (Bank Rate) and longer fixed interest rates are set out in Appendix 4. The following gives the Sector Treasury Services Bank Rate forecast for the next 4 financial year ends (March).

- 2010/2011 0.50%
- 2011/2012 1.00%
- 2012/2013 2.25%
- 2013/2014 3.25%

There is a downside risk to these forecasts especially if recovery from the recession proves to be weaker and slower than currently expected and a short term upside risk should inflation pressures increase. A detailed view of the current economic background is contained within Appendix 5 to this report.

2.6 Borrowing Strategy

2.6.1 Borrowing rates

The Sector forecast in respect of interest rates for loans charged by the PWLB is as follows: -

	M ar-11	Jun-11	Sep-11	Dec-11	M ar-12	M ar-13	M ar-14
Bank rate	0.50%	0.50%	0.50%	0.75%	1.00%	2.25%	3.25%
5yr PW LB rate	3.30%	3.30%	3.40%	3.50%	3.60%	4.30%	5.00%
10yr PW LB rate	4.40%	4.40%	4.40%	4.50%	4.70%	5.10%	5.40%
25yr PW LB rate	5.20%	5.20%	5.20%	5.30%	5.30%	5.50%	5.70%
50yr PW LB rate	5.20%	5.20%	5.20%	5.30%	5.30%	5.50%	5.70%

A more detailed forecast from Sector is included in Appendix 4.

The main sensitivities of the forecast are likely to be;

- 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 borrowing will be undertaken whilst interest rates are still relatively cheap.
- 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 a relapse into recession or, a risk of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

The Council officers, in conjunction with the Council's treasury advisers, will monitor both the prevailing interest rates and the market forecasts.

With long-term interest rate forecasts set to remain around their current levels the Executive Director of Commercial and Corporate Services, taking into account the advice of the Council's treasury adviser considers a benchmark financing rate of 5.50% for any further long-term borrowing for 2011/2012 to be appropriate.

Consideration will be given to various options, including utilising some investment balances to fund the borrowing requirement in 2011/2012. The need to adapt to changing circumstances and revisions to profiling of capital expenditure is required, and flexibility needs to be retained to adapt to any changes that may occur.

The Executive Director of Commercial and Corporate Services, taking advice from the Council's treasury advisers will continue to monitor rates closely, and whilst implementing the borrowing strategy, will adopt a pragmatic approach in identifying the low points in the interest rate cycle at which to borrow.

2.7 Policy on borrowing in advance of need

The Council will not borrow more than or in advance of its needs purely 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 Council can ensure the security of such funds.

In determining whether borrowing will be undertaken in advance of need the Council 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 fully considered;

- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the merits of alternative forms of funding;
- consider alternative interest forecasts available and the most appropriate periods and repayment profiles to use;
- consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk, and other risks, and the level of such risks given the controls in place to minimise them.

2.8 Debt Rescheduling

The reasons for any rescheduling of debt will include:

- the generation of cash savings at minimum risk;
- in order to help fulfil the Treasury Management Strategy; and
- in order to enhance the balance of the long-term portfolio (by amending the maturity profile and/or the balance of volatility).

In previous years, debt rescheduling has achieved significant savings in interest charges and discounts and these interest savings have been secured for many years to come. For example, since November 2008 the Council has rescheduled debt worth £59.5 million with an ongoing reduction in interest costs of just under £1.0 million per annum. The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt, which has now been compounded since 20 October 2010 by a considerable further widening of the difference between new borrowing and repayment rates, has meant that PWLB debt restructuring is much less attractive than it was before both of these measures were introduced. Consideration will also be given to other options where interest savings may be achievable by using LOBO (Lenders Option Borrowers Option) loans, and / or other market loans, in rescheduling exercises rather than solely using PWLB borrowing as the source of replacement financing but this would only be the case where this would represent best value to the Council.

The latest interest rate projections for 2011/2012 show short term borrowing rates will be considerably cheaper than longer term rates and as such there may be potential for some 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 the size of premiums incurred, 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.

The Council is keeping a watching brief on market conditions in order to secure further debt rescheduling when, and if, appropriate opportunities arise. The timing of all borrowing and investment decisions inevitably includes an element of risk, as those decisions are based upon

expectations of future interest rates. The policy to date has been very firmly one of risk spread and this prudent policy will be continued.

Any rescheduling undertaken will be reported to Cabinet, as part of the agreed treasury management reporting procedure.

3. Annual Investment Policy and Strategy

3.1 Investment Policy and Objectives

When considering its investment policy and objectives, the Council has taken regard to the Department of Communities and Local Government's (DCLG) Guidance on Local Government Investments ("the Guidance") and the 2009 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code").

The Council's investment objectives are: -

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

The Council also aims to achieve the optimum return on its investments but commensurate with proper levels of security and liquidity. The risk appetite of the Council is regarded as low in order to give priority to security of its investments.

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

3.2 Investment Strategy

This Strategy sets out:

- the procedures for determining the use of each class of investment (advantages and associated risk), particularly if the investment falls under the category of "non-specified investments";
- the maximum periods for which funds may be prudently committed in each class of investment;
- the amount or percentage limit to be invested in each class of investment;
- whether the investment instrument is to be used by the Council's in-house officers and/or by the Council's appointed external fund managers, (if used); and, if non-specified investments are to be used in-house, whether prior professional advice is to be sought from the Council's treasury advisers;
- the minimum amount to be held in short-term investments (i.e. an investment which the Council may require to be repaid or redeemed within 12 months of making the investment).

3.3 Investment Types

The Council is allowed to invest in two types of investment, namely Specified Investments and Non-specified Investments.

Specified Investments are those investments that are for a period of less than one year, are not classed as capital expenditure, and are placed with high credit rated counterparties.

Non-specified Investments are any investments which are not classified as specified investments. As the Council only uses high credit rated counterparties this means in effect that any investments placed with those counterparties for a period of one year or more will be classed as Non-specified Investments. The Council will not invest in any type of investment that will be classed as capital expenditure (see 3.4 below).

The type of investments to be used by the in-house team will be limited to term deposits, interest bearing accounts, and Money Market Funds and will follow the criteria as set out in Appendix 6.

3.4 Investments Defined as Capital Expenditure

The acquisition of share capital or loan capital in any body corporate is defined as capital expenditure under Section 16(2) of the Local Government Act 2003. Such investments have to be funded out of capital or revenue resources and are classified as 'non-specified investments'.

A loan or grant by this Council to another body for capital expenditure by that body is also deemed by regulation to be capital expenditure by the Council. It is therefore important for the Council to clearly identify if the loan has been made for policy reasons or if it is an investment for treasury management purposes. The latter will be governed by the framework set by the Council for 'specified' and 'non-specified' investments.

The Council will not use (or allow any external fund managers it may appoint to use) any investment which will be deemed as capital expenditure.

3.5 Investment Limits

One of the recommendations of the Code is that local authorities should set limits for the amounts of investments that can be placed with institutions by country, sector and group. These limits are applied in the Council's Counterparty criteria set out in Appendix 6.

The minimum amount of overall investments that the Council will hold in short-term investments (less than one year) is £50 million. As the Council has decided to restrict most of its investments to term deposits, it will maintain liquidity by having a minimum of 30% of these short-term investments maturing within 6 months.

A maximum limit of £100 million is to be set for in-house non-specified investments over 364 days up to a maximum period of 2 years. This amount has been calculated by reference to the Council's cash flows, including the potential use of earmarked reserves. The Executive Director of Commercial and Corporate Services will monitor long-term investment rates and identify any investment opportunities if market conditions change.

3.6 Provisions for Credit Related Losses

If any of the Council's investments appear at risk of loss due to default, (i.e. a credit-related loss, and not one resulting from a fall in price due to movements in interest rates), then the Council will make revenue provision of an appropriate amount in accordance with proper accounting practice or any prevailing government regulations, if applicable. This position has not occurred and the Council mitigates this risk with its prudent investment policy.

3.7 Creditworthiness policy

The creditworthiness policy adopted by this Council takes into account not only the credit ratings issued by all three credit rating agencies (Fitch, Moody's and Standard & Poor's), but also, available market data and intelligence, the level of government support to financial institutions and advice from its Treasury Management advisors.

Set out in Appendix 6 is the detailed criteria that will be used, subject to approval, in determining the level of investments that can be invested with each counterparty or institution. Where a counterparty is rated differently by any of the 3 rating agencies, the lowest rating will be used to determine the level of investment.

3.8 Monitoring of Credit Ratings

- All credit ratings are monitored on a daily basis. The Council has access to all three credit ratings agencies and is alerted to changes through its use of the Sector Treasury Services credit worthiness service.
- If a counterparty's rating is downgraded with the result that it no longer meets the Council's minimum criteria, the Council will cease to place funds with that counterparty. The Council will also immediately inform its external fund manager(s), if used, to cease placing funds with that counterparty.
- If a counterparty's rating is downgraded with the result that, their rating is still sufficient for the counterparty to remain on the Approved Lending List, then the counterparty's authorised investment limit will be reviewed accordingly. A downgraded credit rating may result in the lowering of the counterparty's investment

limit and vice versa. The Council will also immediately inform its external fund manager(s), if used, of any such change(s).

Should fund managers be employed by the Council, the Council will establish with its fund manager(s) their credit criteria and the frequency of their monitoring of credit ratings so as to be satisfied as to their adherence to the Council's policy.

3.9 Past Performance and Current Position

During 2010/2011 the Council did not employ any external fund managers, all funds being managed by the in-house team. The performance of the fund by the in-house team is shown below and compares this with the relevant benchmarks and performance from the previous year:

	2009/10 Return %	2009/10 Benchmark %	2010/11 Return %	2010/11 Benchmark %
			Year to date	Year to date
Council	1.91	0.36	1.49	0.34

During 2010/2011 the Council continues to review the optimum arrangements for the investment of its funds whilst fully observing the investment strategy in place.

3.10 Outlook and Proposed Investment Strategy

Based on its cash flow forecasts, the Council anticipates its fund balances in 2011/2012 are likely to range between £150 million and £300 million. This represents a cautious approach and provides for funding being received in excess of the level budgeted for, and also for unexpected and unplanned levels of capital underspending in the year or re-profiling of spend into future years. In 2011/2012, with short-term interest rates forecast to be materially below long-term rates, it is possible that some investment balances may be used to fund some long-term borrowing or used for debt rescheduling. Such funding is wholly dependent upon market conditions and will be assessed and reported to Cabinet if and when the appropriate conditions arise.

The Council is not committed to any investments, which are due to commence in 2011/2012, (i.e. it has not agreed any forward deals).

Activities likely to have a significant effect on investment balances are:

- Capital expenditure during the financial year, (dependent upon timing), will affect cash flow and short term investment balances;
- Any re-profiling of capital expenditure from, and to, other financial years will also affect cash flow, (no re-profiling has been taken into account in current estimates);
- Any unexpected capital receipts or income;

- Timing of new long-term borrowing to fund capital expenditure;
- Possible funding of long-term borrowing from investment balances (dependent upon appropriate market conditions).

The Executive Director of Commercial and Corporate Services, in conjunction with the Council's treasury adviser Sector Treasury Services, and taking into account the minimum amount to be maintained in short-term investments, will continue to monitor investment rates closely and to identify any appropriate investment opportunities that may arise.

It is proposed that delegated authority continues to be given to the Executive Director of Commercial and Corporate Services, in consultation with the Cabinet Portfolio holder for Resources, to vary the Lending List Criteria and Lending List itself should circumstances dictate, on the basis that changes be reported to Cabinet retrospectively, in accordance with normal Treasury Management reporting procedures.

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

3.11 External fund managers

At present the Council does not employ any external fund managers.

Should the Council appoint any external fund managers in the future, they will have to agree to strict investment limits and investment criteria. These external fund managers will work to the following parameters:

- The institutions on the Approved Lending list of the external manager must correspond to those agreed with Sunderland City Council (i.e. only institutions on Sunderland City Council's Approved Lending List to be included as shown in Appendix 7);
- they will be allowed to invest in term deposits, Certificates of Deposit (CD's) and government gilt securities;
- An investment limit of £3 million per institution (per manager);
- A maximum limit of 50% fund exposure to government gilts;
- A maximum proportion of the fund invested in instruments carrying rates of interest for periods longer than 364 days shall not exceed 50%. Again, it is proposed to only recommend the use of fixed term deposits up to a maximum of 2 years.

3.12 Policy on the use of external service providers

The Council uses Sector as its external treasury management advisers. The Council recognises that responsibility for treasury management decisions remains with the Council 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 Council will ensure that the terms of their

appointment and the methods by which their value will be assessed are properly agreed and documented, and subject to regular review.

4. **Scheme of delegation**

- 4.1 The Treasury Management Strategy Statement has been prepared in accordance with the revised Code. Accordingly, the Council's Treasury Management Strategy (TMS) is approved annually by the full Council and full Council now receive, as a minimum, a mid-year TMS report and an annual Treasury Management outturn report for the previous year by no later than the 30th September of the following year. In addition quarterly reports are made to Cabinet and the Audit and Governance Committee and monitoring reports are reviewed by members in both executive and scrutiny functions respectively. 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.

The Council adopted the following reporting arrangements in accordance with the requirements of the Code: -

Area of Responsibility	Council/ Committee/ Officer	Frequency
Treasury Management Policy Statement (revised)	Full Council	Adoption of the new code for 2010/2011 and then as required
Treasury Management Strategy / Annual Investment Strategy	Full Council	Annually before the start of the year
Treasury Management Strategy / Annual Investment Strategy – mid year report	Full Council	Mid year
Treasury Management Strategy / Annual Investment Strategy –updates or revisions at other times	Full Council	As appropriate
Annual Treasury Management Outturn Report	Full Council	Annually by 30/9 after the end of the financial year
Treasury Management Monitoring Reports	Director of Financial Resources	Monthly
Treasury Management Practices	Director of Financial Resources	Annually
Scrutiny of Treasury Management Strategy	Cabinet / Audit and Governance Committee	Annually before Full Council
Scrutiny of Treasury Management Performance	Cabinet / Audit and Governance Committee	Quarterly

5. **The Treasury Management Role of the Section 151 Officer**

5.1 The Executive Director of Corporate Services is the Council's Section 151 Officer and has specific delegated responsibility in the Council's Constitution to manage the borrowing, financing, and investment requirements of the Council in accordance with the Treasury Management Policy agreed by the Council. This includes;

- 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.

Appendix 4

Interest Rate Forecasts

Introduction

The data below shows a variety of forecasts published by a number of institutions. The first three are individual forecasts from Sector Treasury Services, Capital Economics (an independent forecasting consultancy) and UBS (which represents summarised figures drawn from the population of all major City banks and academic institutions).

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

1. Individual Forecasts

Sector:

Interest rate forecast – 6.1.11

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Bank rate	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%	2.25%	2.75%	3.00%	3.25%	3.25%
3 month LIBID	0.60%	0.70%	0.80%	1.00%	1.25%	1.50%	1.75%	2.00%	2.50%	3.00%	3.25%	3.50%	3.50%
6 month LIBID	0.90%	1.00%	1.10%	1.20%	1.50%	1.80%	2.10%	2.40%	2.80%	3.20%	3.50%	3.80%	4.00%
12 month LIBID	1.40%	1.50%	1.60%	1.80%	2.10%	2.40%	2.70%	3.00%	3.20%	3.40%	3.65%	4.00%	4.20%
5yr PWLB rate	3.30%	3.30%	3.40%	3.50%	3.60%	3.80%	3.90%	4.10%	4.30%	4.60%	4.80%	4.90%	5.00%
10yr PWLB rate	4.40%	4.40%	4.40%	4.50%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%	5.30%	5.40%	5.40%
25yr PWLB rate	5.20%	5.20%	5.20%	5.30%	5.30%	5.40%	5.40%	5.40%	5.50%	5.50%	5.60%	5.70%	5.70%
50yr PWLB rate	5.20%	5.20%	5.20%	5.30%	5.30%	5.40%	5.40%	5.40%	5.50%	5.50%	5.60%	5.70%	5.70%

Capital Economics:

Interest rate forecast – 12.1.11

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13
Bank Rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.50%	2.00%
5yr PWLB rate	3.20%	3.20%	3.00%	2.75%	2.75%	2.90%	3.00%	3.20%	3.40%	3.60%	3.90%	4.20%
10yr PWLB rate	4.75%	4.75%	4.25%	3.75%	3.75%	3.75%	3.75%	3.75%	3.90%	4.00%	4.30%	4.60%
25yr PWLB rate	5.25%	5.25%	4.85%	4.65%	4.65%	4.65%	4.65%	4.65%	4.75%	4.85%	5.10%	5.30%
50yr PWLB rate	5.30%	5.30%	5.20%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.10%	5.20%	5.30%

UBS:

Interest rate forecast (for quarter ends) – 6.1.11

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12
Bank rate	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%	2.00%
10yr PWLB rate	4.30%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%
25yr PWLB rate	5.25%	5.30%	5.35%	5.40%	5.45%	5.50%	5.55%	5.60%
50yr PWLB rate	5.35%	5.40%	5.45%	5.50%	5.55%	5.60%	5.65%	5.70%

2. Survey of Economic Forecasts**HM Treasury January 2011**

The current Q4 2010 and 2011 forecasts are based on the January 2011 report. Forecasts for 2010 – 2014 are based on 32 forecasts in the last quarterly forecast – in November 2010.

BANK RATE FORECASTS		quarter ended		annual average Bank Rate			
	actual	Q4 2011		ave. 2011	ave. 2012	ave. 2013	ave. 2014
Median	0.50%	1.00%		0.90%	1.60%	2.40%	3.00%
Highest	0.50%	1.60%		2.10%	3.10%	3.60%	4.50%
Lowest	0.50%	0.50%		0.50%	0.50%	0.60%	1.20%

Economic Background

1.1. Global economy

The economic downturn that began following the global credit crunch of August 2007 has continued into 2011. The sovereign debt crisis peaked in May 2010 prompted by major concerns over the size of the Greek government's total debt and annual deficit. Any default or write down of Greek debt would have a substantial impact on other countries, in particular, Portugal, Spain and Ireland. This crisis culminated in the EU and IMF putting together a €750bn support package in mid May. A second crisis, this time over Ireland in November 2010, culminated in Ireland also having to take EU support. There is a concern that Portugal will also shortly need to take EU support. That, in turn, would then cause further major concerns as to whether the current size of the support package facility put together by the EU and IMF would be big enough to cope with any crisis involving another major economy.

The unexpectedly high rate of growth in quarters 2 and 3 of 2010 in the UK and the Euro zone in Q2 were driven by strong growth in the construction sector catching up from inclement weather earlier in the year and by other short term factors. General expectations are for low (but not negative) growth in 2011 in the western economies.

1.2 UK economy

Following the general election in May 2010, the coalition government has put in place austerity measures to carry out a 'correction' of the public sector deficit over the next five years. The result of fiscal contraction will be major job losses during this period, in particular, in public sector services. This will have a knock-on effect on consumer and business confidence and appears to have also hit the housing market as house prices started on a negative trend during the summer and autumn of 2010. Mortgage approvals are also at very weak levels and are declining, all of which indicates that the housing market is likely to be very weak in 2011.

Economic Growth – GDP growth is likely to have peaked in the current period of recovery at 1.2% in quarter 2 of 2010. Growth in quarter 3 at +0.7% was also unexpectedly high. However, the outlook is for low growth in 2011/2012 although the Bank of England and the Office for Budget Responsibility are forecasting near trend growth (2.5%) i.e. above what most forecasters are currently expecting.

Unemployment – the trend of falling unemployment (on the benefit claimant count) has been replaced since July 2010 with small increases which are likely to be the start of a new trend for some years ahead of rising unemployment.

Inflation and Bank Rate – CPI has remained high during 2010. It peaked at 3.7% in April gradually declined to 3.1% in September but has now returned to the level of 3.7% in December (RPI 4.7%). Although inflation

has remained above the MPC's 2% target, the MPC is confident that inflation will fall back under the target over the next two years.

The Bank of England finished its programme of quantitative easing (QE) with a total of £200bn in November 2009. However, expectations that there could be a second round of quantitative easing in early 2011, to help support economic growth, have evaporated after the surprises of the Q3 GDP figure of +0.7% and the outcome of the November Inflation Report revising the forecast for short-term inflation sharply upwards.

Sector's view is that there is unlikely to be any increase in the Bank Base Rate until the end of 2011.

AAA rating – prior to the general election, credit rating agencies had issued repeated warnings that unless there was a major fiscal contraction, then the AAA sovereign rating was at significant risk of being downgraded. Sterling was also under major pressure during the first half of the year. However, after the Chancellor's Emergency Budget on 22nd June 2010, Sterling strengthened against the US dollar and confidence has returned that the UK will retain its AAA rating. In addition, international investors now view UK government gilts as being a safe haven from EU government debt. The consequent increase in demand for gilts helped to add downward pressure on gilt yields and PwLB rates.

1.3 Economic Forecast

It is currently difficult to have confidence as to exactly how strong the UK economic recovery is likely to be, and there are a range of views in the market. Sector Treasury Services has adopted a moderate view. There are huge uncertainties in all forecasts due to the major difficulties of forecasting the following areas:

- the speed of economic recovery in our major trading partners - the US and EU
- the danger of a currency war and a resort to protectionism and tariff barriers if China does not address the issue of its huge trade surplus due to its undervalued currency
- the degree to which government austerity programmes will dampen economic growth and undermine consumer confidence
- changes in the consumer savings ratio
- the speed of rebalancing of the UK economy towards exporting and substituting imports
- the potential for more quantitative easing, and the timing of this in both the UK and US, and its subsequent reversal
- the speed of recovery of banks' profitability and balance sheet imbalances and the consequent implications for the availability of credit to borrowers
- the potential for a major EU sovereign debt crisis which could have a significant impact on financial markets and the global and UK economy

The overall balance of risks is weighted to the downside and there is some risk of a double dip recession, creating a downward spiral of falling

demand, falling jobs and falling prices, although this is currently viewed as being a small risk. Sector believes 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.

Counterparty Criteria

The Council takes into account not only the individual institution's credit ratings issued by all three credit rating agencies (Fitch, Moody's and Standard & Poor's), but also all available market data and intelligence, the level of government support and advice from its Treasury Management advisors.

Set out below are the criteria to be used in determining the level of funds that can be invested with each institution. Where an institution is rated differently by the rating agencies, the lowest rating will determine the level of investment.

Fitch / S&P's Long Term Rating	Fitch Short Term Rating	S&P's Short Term Rating	Moody's Long Term Rating	Moody's Short Term Rating	Maximum Deposit £m	Maximum Duration
AAA	F1+	A1+	Aaa	P-1	50	2 Years
AA+	F1+	A1+	Aa1	P-1	50	2 Years
AA	F1+	A1+	Aa2	P-1	40	364 days
AA-	F1+ / F1	A1+ / A-1	Aa3	P-1	20	364 days
A+	F1	A-1	A1	P-1	10	364 days
A	F1 / F2	A-1 / A-2	A2	P-1 / P-2	10	364 days
A-	F1 / F2	A-2	A3	P-1 / P-2	5	6 months
Local Authorities (limit for each local authority)					30	364 Days
Money Market Funds Maximum amount to be invested in Money Market Funds is £50 million with a maximum of £30 million in any one fund.					50	2 Years

Where the UK Government holds a shareholding in an institution the UK Government's credit rating of AAA will be applied to that institution to determine the amount the Council can place with that institution.

Where any banks / building societies are part of the UK Government's Credit Guarantee scheme (marked with * in the Approved Lending List), these counterparties will have an AA rating applied to them thus giving them a credit limit of £40 million for a maximum period of 364 days

The Code of Practice for Treasury Management in the Public Services recommends that consideration should also be given to country, sector, and group limits in addition to the individual limits set out above, these new limits are as follows:

Appendix 6 (continued)

Country Limit

It is proposed that only countries with a minimum sovereign credit rating of AA+ by all three rating agencies will be considered for inclusion on the Approved Lending List.

It is also proposed to set a total limit of £40 million which can be invested in other countries provided they meet the above criteria. A separate limit of £300 million will be applied to the United Kingdom and is based on the fact that the government has done and is willing to take action to protect the UK banking system.

Country	Limit £m
UK	300
Non UK	40

Sector Limit

The Code recommends a limit be set for each sector in which the Council can place investments. These limits are set out below:

Sector	Limit £m
Central Government	300
Local Government	300
UK Banks	300
UK Building Societies	150
Foreign Banks	40

Group Limit

Where institutions are part of a group of companies e.g. Lloyds Banking Group, Santander and RBS, then total limit of investments that can be placed with that group of companies will be determined by the highest credit rating of a counterparty within that group, unless the government rating has been applied. This will apply provided that:

- the government's guarantee scheme is still in place;
- the UK continues to have a sovereign credit rating of AAA; and
- that market intelligence and professional advice is taken into account.

Proposed group limits are set out in Appendix 7

Approved Lending List

Appendix 7

	Fitch				Moody's			Standard & Poor's		Limit £m	Max Deposit Period
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength	L Term	S Term		
UK	AAA	F1+			Aaa			AAA		300	364 days
Lloyds Banking Group (see Note 1)										Group Limit 50	
Lloyds Banking Group plc	AA-	F1+	C	1	Aa3	-	-	A	A-1	50	364 days
Lloyds TSB Bank Plc	AA-	F1+	C	1	Aa3	P-1	C-	A+	A-1	50	364 days
Bank of Scotland Plc	AA-	F1+	C	1	Aa3	P-1	D+	A+	A-1	50	364 days
Royal Bank of Scotland Group (See Note 1)										Group Limit 50	
Royal Bank of Scotland Group plc	AA-	F1+	C/D	1	A1	P-1	-	A	A-1	50	364 days
The Royal Bank of Scotland Plc	AA-	F1+	C/D	1	Aa3	P-1	C-	A+	A-1	50	364 days
National Westminster Bank Plc	AA-	F1+	-	1	Aa3	P-1	C-	A+	A-1	50	364 days
Ulster Bank Ltd	A+	F1+	E	1	A2	P-1	D-	A	A-1	50	364 days
Santander Group *										Group Limit 40	
Santander UK plc	AA-	F1+	B	1	Aa3	P-1	C-	AA	A-1+	40	364 days
Cater Allen	AA-	F1+	B	1	Aa3	P-1	C-	AA	A-1+	40	364 days
Barclays Bank plc *	AA-	F1+	B	1	Aa3	P-1	C	AA-	A-1+	40	364 days
HSBC Bank plc *	AA	F1+	B	1	Aa2	P-1	C+	AA	A-1+	40	364 days

Appendix 7(continued)

	Fitch			Moody's				Standard & Poor's		Limit £m	Max Deposit Period
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength	L Term	S Term		
Nationwide BS *	AA-	F1+	B	1	Aa3	P-1	C-	A+	A-1	40	364 days
Standard Chartered Bank *	AA-	F1+	B	1	A2	P-1	C+	A+	A-1	40	364 days
Clydesdale Bank / Yorkshire Bank **	AA-	F1+	C	1	A1	P-1	C-	A+	A-1	10	364 days
Co-Operative Bank Plc	A-	F2	B/C	3	A2	P-1	D+	-	-	5	6 months
Northern Rock ***	BBB+	F2	C	2	-	-	-	A-	A-2	0	
Top 10 Building Societies (by asset value)											
Nationwide BS (see above)											
Yorkshire BS	A-	F2	B/C	5	Baa1	P-2	D+	A-	A-2	0	
Coventry BS	A	F1	B	5	A3	P-2	C-	-	-	5	6 Months
Skipton BS	A-	F2	B/C	5	Baa1	P-2	D+	-	-	0	
Leeds BS	A	F1	B/C	5	A2	P-1	C+	-	-	10	364 Days
West Bromwich BS ***	BBB-	F3	C/D	5	Baa3	P-3	E+	-	-	0	
Principality BS ***	BBB+	F2	C	5	Baa2	P-2	D-	-	-	0	
Newcastle BS ***	BBB-	F3	C/D	5	Baa2	P-2	D-	-	-	0	
Norwich and Peterborough BS ***	BBB+	F2	C	5	Baa2	P-2	D	-	-	0	
Nottingham BS	-	-	-	-	A3	P-2	C-	-	-	5	6 Months
Foreign Banks have a combined total limit of £40m											
Australia	AA+	-	-	-	Aaa	-	-	AAA		40	364 Days
National Australia Bank	AA	F1+	B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
Australia and New Zealand Banking Group Ltd	AA-	F1+	B	1	Aa1	P-1	B	AA	A-1+	20	364 Days

Appendix 7 (continued)

	Fitch				Moody's			Standard & Poor's		Limit £m	Max Deposit Period
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength	L Term	S Term		
Commonwealth Bank of Australia	AA	F1+	A/B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
Westpac Banking Corporation	AA	F1+	A/B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
Canada	AAA				Aaa			AAA		40	364 Days
Bank of Nova Scotia	AA-	F1+	B	1	Aa1	P-1	B	AA-	A-1+	20	364 Days
Royal Bank of Canada	AA	F1+	A/B	1	Aa1	P-1	B+	AA-	A-1+	20	364 Days
Toronto Dominion Bank	AA-	F1+	B	1	Aaa	P-1	B+	AA-	A-1+	20	364 Days
Money Market Funds										50	2 Years
Prime Rate Stirling Liquidity	AAA MMF							AAAm		30	2 Years
Insight Liquidity Fund					AAA MR1			AAAm		30	2 Years
Ignis Sterling Liquidity	AAA MMF							AAAm		30	2 Years

Notes

Note 1

Nationalised / Part Nationalised

The counterparties in this section will have the UK Government's AAA rating applied to them thus giving them a revised credit limit of £50 million for a maximum period of 364 days

* Banks / Building Societies which are part of the UK Government's Credit Guarantee scheme

The counterparties in this section will have an AA rating applied to them thus giving them a revised credit limit of £40 million for a maximum period of 364 days

** The Clydesdale Bank (under the UK section) is owned by National Australia Bank

*** These will be revisited and used only if they meet the minimum criteria (ratings of A- and above)

Any bank which is incorporated in the United Kingdom and controlled by the FSA is classed as a UK bank for the purposes of the Approved Lending List.

